

REPUBLIC OF KENYA
IN THE HIGH COURT OF KENYA AT NAIROBI
MILIMANI LAW COURTS
COMMERCIAL AND TAX DIVISION
COMM CASE NO. E415 OF 2024

BETWEEN

RONY DARAYAS

GANDHI.....PLAINTIFF

AND

DEVAL KANAIYALAL MODI1ST

DEFENDANT

KENDIA POLYPACK LIMITED.....2ND

DEFENDANT

RULING

INTRODUCTION AND BACKGROUND

1. The Court is being called upon to determine three applications by the Plaintiff (RONY); The Notice of Motion dated 26th July 2024 that seeks leave to institute a derivative suit on behalf of the 2nd Defendant (“the Company”), injunctive orders against the 1st Defendant (DEVAL) restraining him from *inter alia* convening Company meetings, taking unilateral decisions, dealing with Company funds, or disposing of his shares and; the appointment of an audit firm for a forensic audit of the Company since

incorporation. There is also the Notice of Motion dated 30th July 2024 that seeks to restrain DEVAL from disposing of his shares in the Company and from dealing with funds in his personal bank account at *Diamond Trust Bank* account number 0*****001. Lastly, is the Notice of Motion dated 9th August 2024 that seeks to restrain DEVAL from any travels outside the territorial jurisdiction of the Court.

2. The applications are supported by grounds set out on their faces together with RONY's affidavits sworn on 26th July 2024, 30th July 2024, 9th August 2024 and 16th September 2024. They are opposed by DEVAL through his replying affidavits sworn on 29th August 2024 and 18th October 2024. The applications were canvassed by way of written submissions which I have considered and I will be making relevant references to the same in my analysis and determination below.

ANALYSIS AND DETERMINATION

3. From RONY's applications and submissions, he seeks the Court to determine three issues:

- a) *Whether RONY has satisfied the test for grant of leave to institute a derivative action suit on behalf of the Company.*

b) Whether the applications meet the test for grant of the interim injunctive reliefs sought; and

c) Whether the Court should grant orders restraining DEVAL from travelling outside the Jurisdiction

DERIVATIVE ACTION SUIT ON BEHALF OF THE COMPANY

4. RONY states that he is a minority shareholder of the Company and seeks to continue with the derivative suit on behalf of the Company and that the action is against the majority shareholder and that he also seeks reliefs for the Company. He claims that DEVAL has completely shut him out of the Company's management and refuses to share operational, financial, or strategic information. DEVAL is accused of embezzling company funds for personal use., using a "secret and parallel accounts" system to siphon off cash payments, transferring Company money to other companies owned solely by himself or his proxies and unilaterally passing a resolution to liquidate the Company without RONY's proper involvement.
5. RONY further states that after agreeing to sell a Company property to settle a Kshs 35 million debt to RONY, DEVAL issued a notice to sell his shares. RONY claims this is a tactic to evade the Company's and his personal liabilities, including a Kshs. 35 million tax debt with the Kenya Revenue Authority (KRA). DEVAL is accused of acting in his

own interest, contrary to his duties as a director, and in violation of the Company's Articles of Association.

6. In response, DEVAL refutes RONY's claim that he was excluded from management. He states that RONY was actively involved in day-to-day operations, had access to bank statements, and was a signatory to Company accounts. He accuses RONY of contradicting himself by alleging non-involvement while also referencing his own participation in company negotiations for example with KRA and *M-Oriental Bank*. DEVAL denies all allegations of embezzlement, misappropriation, or running proxy accounts. Instead, he accuses RONY of setting up a competing business, which harmed the Company and he also alleges that RONY withdrew Company funds without authorization from *Equity Bank* and *M-Oriental Bank* accounts.
7. DEVAL admits that a Company car was transferred to his name, but says this was done with RONY's knowledge and as part of an agreement linked to the sale of a warehouse. He denies privatizing company assets and states that all transactions were documented and known to RONY. He confirms the Company ceased operations in 2023 due to financial difficulties and liabilities exceeding assets. DEVAL confirms that a resolution to liquidate the Company was

passed by both directors but he denies the existence of any agreement to pay off RONY and states that RONY is not a creditor of the Company. DEVAL confirms that the Company entered into an Alternative Dispute Resolution (ADR) Agreement with KRA on 25th June 2024 and he states that RONY was actively involved in the negotiations and signed the agreement. That the Company has been unable to meet the payment plan due to ceased operations and DEVAL argues that RONY has not met the legal threshold for a derivative action. He claims RONY did not demonstrate that he tried to bring the action in the Company's name or that he was prevented by the majority.

8. I do not think it is in dispute that whether the Court should grant permission to

the RONY to proceed with this suit as a derivative suit is governed by **sections 238**

and **239** of the ***Companies Act(Chapter 486 of the Laws of Kenya)*** which

provides as follows:

*238 (1) In this Part, "derivative claim" means proceedings by
a member of a company—*

(a) *in respect of a cause of action vested in the company; and*

(b) *seeking relief on behalf of the company.*

(2) *A derivative claim may be brought only—*

(a) *under this Part; or*

(b) *in accordance with an order of the Court in proceedings for protection of members against unfair prejudice brought under this Act.*

(3) A derivative claim under this Part may be brought only in respect of a cause of action arising from an actual or proposed act or omission involving negligence, default, breach of duty or breach of trust by a director of the company.

(4) A derivative claim may be brought against the director or another person, or both.

(5) It is immaterial whether the cause of action arose before or after the person seeking to bring or continue the derivative claim became a member of the company.

(6) *For the purposes of this Part—*

(a) *"director" includes a former director;*

(b) *a reference to a member of a company includes a person who is not a member but to whom shares in the company have been transferred or transmitted by operation of law.*

239. *Application for permission to continue derivative claim*

(1) *in order to continue a derivative claim brought under this Part by a member, the member has to apply to the Court for permission to continue it.*

- (2) *If satisfied that the application and the evidence adduced by the applicant in support of it do not disclose a case for giving permission, the Court—*
- (a) *shall dismiss the application; and*
 - (b) *may make any consequential order it considers appropriate,*
- (3) *If the application is not dismissed under subsection (2), the Court—*
- (a) *may give directions as to the evidence to be provided by the company; and*
 - (b) *may adjourn the proceedings to enable the evidence to be obtained.*
- (4) *On hearing the application, the Court may—*
- (a) *give permission to continue the claim on such terms as it considers appropriate;*
 - (b) *refuse permission and dismiss the claim; or*
 - (c) *adjourn the proceedings on the application and give such directions as it considers appropriate.*
- [Emphasis mine]

9. The aforesaid provisions provide the framework for instituting claims by members of the Company on behalf of the Company. Prior to the enactment of the **Companies Act**, such suits were governed by the rule in **Foss v Harbottle [1843] 67 ER 189** which established the general principal that a wrong alleged to have been done to a company, can only be remedied by an action by the company itself. However, several exceptions to the rule developed including the

derivative action process which allowed a minority shareholder to bring a claim on behalf of the Company.

10. I agree with RONY's submissions that the late Onguto J., in **Ghelani Metals Limited, Ghelani Enterprises Limited, Tononoka Fireworks Limited & Jayshree Suchak Sanjiv v Elesh Ghelani Natwarlal & Registrar of Companies [2017] KEHC 4629 (KLR)** explained the effect of the **Companies Act** on the common law rule in **Foss v Harbottle (Supra)** as follows:

44. *Statutory procedure is now the exclusive method of pursuing derivative claims. The Act sets out what sorts of company claims may be pursued and is also explicit that derivative claims may only be pursued under the Act. The question must only be the factors the Court ought to consider before approving a derivative claim.*

45. *There appears, in my view, to exist a two-stage process. The Court must first satisfy itself that there is a prima facie case on any of the causes of action noted under s.238(3). S.239(2) of the Act provides that the application for permission will be dismissed if the evidence adduced in support "do not disclose a case" for giving of permission. The essence of judicial approval under the Act is to screen out frivolous claims. The Court is only to allow meritorious claims. All that the applicant needs to establish, through evidence, is a prima facie case without the need to show that it will succeed.*

11. That an Applicant ought to establish a *prima facie* case was affirmed by the Court of Appeal in **Amin Akberali Manji, Hemanth Kumar & Musikland Millenium Limited v Altaf Abdulrasul Dadani & Musikland Limited (Under Receivership) [2015] KECA 356 (KLR)**. In considering whether to grant permission, the Court is also guided by **section 241** of the **Companies Act** which sets out circumstances under which the Court shall refuse the application and the considerations the Court shall take into account when granting permission to the applicant to continue the suit as a derivative suit. The section provides as follows:

241. (1) *If a member of a company applies for permission under section 239 or 240, the Court shall refuse permission if satisfied—*

(a) *that a person acting in accordance with section 144 would not seek to continue the claim;*

(b) *if the cause of action arises from an act or omission that is yet to occur—that the act or omission has been authorized by the company;*

(c) *if the cause of action arises from an act or omission that has already occurred — that the act or omission*

—
(i) *was authorised by the company before it occurred; or*

(ii) has been ratified by the company since it occurred.

(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) authorised 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 member's 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.*

[Emphasis mine]

12. DEVAL has also rightly cited the decision in **Isaiah Waweru Ngumi & 2 others v Muturi Ndung'u [2016] KEHC 3032 (KLR)** where Ngugi J.,(as he was then) summarised some of the factors to be considered in granting permission to commence or continue a derivative action as follows:

[21]...Among other things, the Court considers the following factors:

(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 v 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 complaint is one of lack of authority by the shareholders or the company - is likely to be authorised 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.

13. I have gone through the grounds presented by RONY in his application and DEVAL's rebuttal and I find that RONY has not demonstrated a *prima facie* case against DEVAL. On the ground that he has been excluded from the Company's management, DEVAL has demonstrated that RONY has been involved in the Company's affairs, as evidenced by his participation in the ADR with KRA that took place early in 2024(DKM-2 and DKM-3). He has also annexed

the Company's financial statements (*DKM-4*) from 2016-2022 that are signed by both directors, indicators and evidence that places RONY at the heart of significant Company transactions, directly contradicting the claim of exclusion. I also do not find concrete evidence of misappropriation and embezzlement of the Company's assets and funds as the allegations of DEVAL transferring funds to proxies or having secret accounts are unsupported. It has also not been substantially denied that the Company's bank accounts and signing mandates are that of "either-or" which allows RONY or DEVAL to make unilateral withdrawals. No evidence has been shown that the withdrawals by DEVAL were being used for personal benefit rather than the Company's.

14. On the sale of his shares to avoid the Company's liability, I am in agreement with DEVAL that selling his shares was a lawful exercise of his rights as per the Company's Memorandum and Articles of Association. He correctly states that a company is a separate legal entity and its liabilities are not the personal liabilities of shareholders, so selling shares does not distance him from the Company debts. DEVAL has demonstrated that he even issued a notice of pre-emption rights to RONY.

15. It is for the above reasons that I find that no *prima facie* case has been made out by RONY for the grant of permission to proceed with this suit as a derivative action on behalf of the Company. It is evident from the affidavits of both parties that the relationship between the only two directors and shareholders of the Company has irretrievably broken down. The allegations are acrimonious, mutual, and speak to a complete loss of trust and confidence. The Company has ceased operations since 2023, and the directors are at an impasse regarding its future. This situation constitutes a classic deadlock. In such circumstances, the substratum of the company, the mutual trust and cooperation essential for its functioning, has disappeared. It is no longer feasible for the Company to be managed in a manner that serves the interests of its shareholders or its stated purpose. The parties should consider winding up the Company as it will be just and equitable to do so in light of the present circumstances.

16. Consequent to my findings above, it follows that RONY is not entitled to the injunctive reliefs sought or the order seeking to restrain DEVAL from leaving the country. Furthermore, RONY included prayers seeking orders to compel the production of the Company's financial records, books of account, and audit reports. DEVAL has

annexed to his deposition the audited financial statements for the Company from the years 2016 to 2022, all of which were signed by both directors, including RONY himself. DEVAL has also averred, without meaningful contradiction, that RONY has at all material times been in receipt of all bank statements and financial information. In light of this, the Court finds that DEVAL has sufficiently demonstrated that the financial records sought by RONY are not only available but have been in his possession or are readily available to him. Therefore, RONY's prayers seeking to compel the production of these documents are rendered wholly unnecessary.

CONCLUSION AND DISPOSITION

17. In the upshot, the Plaintiff's Notice of Motion Applications dated 26th July 2024, 30th July 2024 and 9th August 2024 are hereby dismissed in their entirety foregoing. The interim orders in place are hereby vacated and/or discharged. The Plaintiff shall bear the costs of all applications.

DATED SIGNED and DELIVERED virtually at NAIROBI this 7TH DAY of NOVEMBER 2025

.....
J.W.W. MONGARE
JUDGE

IN THE PRESENCE OF

1. Mr. Onyinkwa for the Applicant.
2. Mr. Kibet holding brief for Mr. Ndichu for the 1st Respondent.
3. Amos - Court Assistant

ORIGINAL