IN THE COURT OF APPEAL

AT NAIROBI

(CORAM: WARSAME, M'INOTI & MURGOR, JJA)

CIVIL APPEAL NO. 278 OF 2017

(As Consolidated with Appeals Nos.279 and 281 of 2017)

BETWEEN

EQUITY BANK KENYA LIMITED……..…..…..…..APPELLANT

AND

KENYA AIRWAYS PLC…….…..…..1ST RESPONDENT

THE CABINET SECRETARY TO THE NATIONAL TREASURY..2ND RESPONDENT

ECOBANK KENYA LIMITED…….....…..3RD RESPONDENT

THE CO-OPERATIVE BANK OF KENYA LIMITED…….....…4TH RESPONDENT

COMMERCIAL BANK OF AFRICA LIMITED.....5TH RESPONDENT

NATIONAL BANK OF KENYA LIMITED..….....…6TH RESPONDENT

KCB BANK KENYA LIMITED…….....…..……...7TH RESPONDENT

NIC BANK LIMITED…….....…..…….8TH RESPONDENT

DIAMOND TRUST BANK KENYA LIMITED…….....…..…...9TH RESPONDENT

I&M BANK LIMITED…….…….....…..10TH RESPONDENT

CHASE BANK (KENYA) LIMITED (IN RECEIVERSHIP.….....11TH RESPONDENT

JAMII BORA BANK LIMITED…….....…..…12TH RESPONDENT

(*An appeal from the ruling of the High Court of Kenya at Nairobi (Ochieng, J) dated 31st July 2017 in Misc. Petition No 321 of 2017*)

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JUDGMENT OF THE COURT

The 1st respondent, Kenya Airways PLC, is heavily in debt and is unable to meet its financial obligations. All the other parties in these appeals are its unsecured creditors. By a petition dated 17th July 2017, the 1st respondent submitted to the High Court a proposed Scheme of Arrangement under section 926 of the Companies Act, 2015. It also filed an application in which it sought, among others, an order directing a meeting of its creditors be convened on 1st August 2017 for purposes of deliberating and voting on the scheme proposal, and appointment of ***Mr. Mbuvi Ngunze***, or in his absence, ***Mr. Richard Harney***, the Managing partner of Coulson Harney LLP, Advocates, as the chairman of the scheme creditors' meeting.

By an *ex parte* order made on 17th July 2017 the High Court (Ochieng, J.), granted the application and directed, among others, that the meeting of the 1st respondent's creditors to be convened on 1st August 2017 and that the said meeting be chaired as prayed. The learned judge however gave the other parties leave to apply. Three of the parties, namely ***Equity Bank Kenya Limited (the 1st appellant), Ecobank Kenya Limited (the 2nd appellant)*** and ***Jamii Bora Bank Limited (the 3rd appellant),*** were aggrieved by the orders of 17th July 2017 and applied to set them aside. By a ruling dated 31st July 2017, the learned judge dismissed the applications, prompting the three parties to file separate appeals to this Court. We directed, with the consent of the parties, that those appeals be consolidated and heard together as they raised substantially similar issues and arose from the same transaction.

It is common ground that the 1st respondent is in the process of restructuring in an effort to secure additional capital that will see it continue as a going concern. The Companies Act provides a mechanism under which a company may enter into a scheme of arrangement with its creditors. Under ***section 926*** of the Act, a company may present a compromise or arrangement to the court for sanction where a majority of the creditors, or the members voting at a meeting, convened in accordance with ***section 923*** have agreed to the compromise or arrangement. That scheme would be sanctioned if it were approved by at least 75% of the creditors in value. With respect to the scheme that sparked the appeal presently before us, the stake of the ***Government of Kenya***, represented by the ***Cabinet Secretary to the Treasury (the 2nd respondent's),*** and also in the ***National Bank of Kenya Limited (6th respondent)*** and ***Kenya Commercial Bank Limited (7th respondent)***, the scheme would attain 87% approval from the creditors. The appellants therefore maintain that in the circumstances, the scheme is a *fiat accompli* and a violation of the rights as creditors.

The appellants submit first that the learned judge erred by granting the orders of 17th July 2017 *ex parte* without affording them an opportunity to be heard. They submit that the proceedings on that day were in breach of the rules of natural justice and are therefore null and void. They also contend that the learned judge erred in upholding the classification of the creditors, which was improper as they are not all in the same class as is contemplated by ***section 923*** of the of ***the Companies Act***. They add that the 2nd respondent, representing the Government of Kenya, is the single largest creditor of the 1st respondent, having an unsecured sum of US$ 261,000,000.00 in respect of both the principal sum lent and interest. In addition, it is the single largest shareholder as it has 29.8% shares in the 1st respondent, and having issued a sovereign bond to secure the creditors, the Government is therefore a guarantor in the scheme. The Government is also in a different position, they urge, because it is involved in the 1st respondent in various capacities: the Cabinet Secretary of the National Treasury sits in the Board of Directors of the 1st respondent and is currently represented on the Board by the principal secretary of the National Treasury and further that the 2nd respondent approves all the other Board members of the 1st respondent.

Above all this, the appellants argue that they are commercial banks regulated by the ***Central Bank of Kenya*** and are therefore subject to certain regulatory requirements that the 2nd respondent is not subject to. As such, the 2nd respondent cannot fairly serve their interests. In their view, the Government's interest in this case is contrary to the interests of the commercial banks because the 2nd respondent is not interested in a commercial return, while the commercial banks are, because they are dealing with depositor's funds and have to answer to their shareholders. Moreover, the 2nd respondent is at a further advantage because the Government of Kenya is majority shareholder in the 6th and 7th respondents. According to the appellants therefore, the creditors do not have a commonality of interests and at the very least the Government shareholding in the 6th and 7th respondent should be discounted.

In their view, there ought to be a separate meeting of similarly placed creditors, namely the commercial banks who belong to a similar class with commonalty of rights. The appellants argue that the scheme as proposed is unworkable and that persons whose rights are so dissimilar that they cannot sensibly consult together with a view to their common interest must be given separate meetings. For this proposition, they rely on sections 922 and 923 of the Companies Act as well as the case of ***Royal Bank of Scotland NV & Others v. TT International Ltd & Anothe***r ***[2012] SGCA 9***, where the Court of Appeal of Singapore stated that issues regarding separate meetings should be determined at the outset.

The appellants also object to the manner in which the scheme and the proceedings in the High Court were carried out, claiming that the draft scheme was never presented for detailed discussions and deliberations between the creditors. In their view, the 1st respondents' approach will simply see the meeting proceed and the court sanction the scheme as a formality. They also challenge the choice of chairperson of the creditors meeting, submitting that Mr. Ngunze and Mr. Harney are not impartial. They contend that the former was the 1st respondent's CEO when it ran into financial doldrums and that the later is the restructuring adviser of the 1st respondent. On the authority of ***Royal Bank of Scotland NV & Others v. TT International Ltd*** & ***Another (supra),*** it is submitted that as the scheme chairman's duties are quasi judicial, he must be independent, fair and impartial.

The appellants contend further that even if they attend the scheme meeting, they will have no opinion or option because they would only be required to endorse the scheme. This is what they flag out as the most important reason to reclassify the parties so that there is the possibility of genuine discussion and a more just scheme. Under the current scheme, they submit, the Government will have a controlling stake in the proposed scheme and the other creditors will not be allowed to exercise any other option. They add that the guarantee given by the Government has been modified to the detriment of the other creditors. It is therefore important, in their view, to reclassify the creditors before the scheme takes effect.

Lastly the appellants opine that in the circumstances of this case where as it were they stand to be railroaded by the Government, the scheme is a violation of their right to property guaranteed by Article 40 of the Constitution. They also ask us to find that the scheme is not viable and is at variance with the approval and resolution of the National Assembly.

The respondents on the other hand, oppose the appeals. In their view, the High Court did not err in granting the initial order *ex parte* because of the circumstances of the case. They also contend the scheme is not in violation of the appellant's right to property because it is not an arbitrary deprivation of property.

On the main issue of classification of creditors, they submit that the learned judge did not err because the Government, the appellants and the other commercial banks have similar rights as creditors. The 1st respondent relies ***Sovereign Life Assurance Company v. Dodd (In Liquidation) [1892] 2 Q.B. 573*** in which it was stated that:

"a class must be confined to those persons whose rights are not so dissimilar as to make it impossible for them to consult together with a view to their common interest."

The respondents contend that all the creditors have a common interest which is to be paid the money that they had lent to the 1st respondent and to achieve that they have to avoid the insolvency of the 1st respondent. They further submitted that the fact that the government is a shareholder in the 1st respondent does not undermine its status or its rights as an unsecured lender because under the proposed scheme, all the creditors would be treated the same way. The respondents further contend that the fact that the Government holds more shares than the other creditors is a non-issue. They rely on the cases of ***Re Jax Marine Pty Ltd [1967] 1 NSWR 145***, ***Re Telewest Communications PLC (No. 1) [2004] EWHC 924*** and

Primacom Holdings GmbH v Credit Agricole [2011] EWHC 1104 (Ch) in support of the proposition that the fact that a creditor is a shareholder is not a good reason for reclassification.

We have anxiously considered the record of appeal, the ruling of the High Court, the written and oral submissions by the parties and the illuminating authorities that they relied upon. In our estimation, the

parties have irregularity invited us to make pronouncements on a number of issues, which with respect, properly fall for determination, in the first instance, by the meeting of creditors. Issues such as the import and viability of the options presented in the scheme; the terms and conditions of the scheme; whether the scheme should provide for payment of fees to the scheme consultants in priority over creditors; consistency of the scheme with the approval and resolution of the National Assembly; whether the scheme options constitute a violation of the appellants' statutory obligations, including under the Central Bank of Kenya Act; among others, cannot be determined by the courts at this stage. The courts must avoid usurping the mandate of the meeting of creditors by purporting to make decisions on their behalf in the first instance, for the simple reason that creditors are generally the best judges of what is in their own commercial interest. (See ***Re Stemcor (SEA) Pte Ltd [2014] 2 BCLC 373)***. Many of those issues, if they are still outstanding as issues, will have to be determined first by the High Court at the sanction meeting, before coming to this Court in the event any party is dissatisfied by the decision of the High Court. Accordingly, we do not intend to wade into those issues at this stage.

We would readily agree with the appellants that in highly contentious matters as those involved in this appeal, the High Court ought not to readily grant orders *ex parte*. It should only do so if all the parties consent or after they have been afforded an opportunity to be heard. But that is not to say that the High Court has no jurisdiction to grant orders *ex parte,* depending on the circumstances of each case. In the appeal before us, the learned judge considered the circumstances and was persuaded that an *ex parte* order was merited. He also granted the appellants leave to apply, if they were aggrieved by the *ex parte* order, which they duly did and were fully heard before the learned judge delivered the ruling which is the subject of this appeal. All that happened before the meeting that the learned judge had authorized could take place. In our view in deciding to make the *ex parte* order on 17th July 2017, the learned judge was exercising a judicial discretion with which we cannot interfere absent evidence that he was clearly wrong, or that he misdirected himself by acting on matters which he should not have acted on, or failing to take into consideration matters which he should have taken into consideration. (See ***Mbogo & Another v. Shah [1968] EA 93).***

We are not persuaded that the impugned provisions of ***Part XXXIV*** of the Companies Act on ***Compromises, Arrangements, Reconstructions and Amalgamations*** are inconsistent with Article 40(2) of the Constitution and are therefore null and void in terms of Article 2(4) of the Constitution. Article 40(2) prohibits Parliament from enacting a law that permits the State or any person to ***arbitrarily*** deprive a person of property or to limit or restrict enjoyment of the right to property on discriminatory grounds such as race, sex pregnancy, ethnic or social origins, among others. In our view the impugned provisions do not allow arbitrary deprivation or expropriation of property; all that they do is, to provide a mechanism for saving a deserving enterprise under financial stress and guaranteeing vulnerable creditors ultimately payment. The reasons underpinning the rescue mechanism are eminently reasonable and rational and justifiable in an open democratic state based on human rights. The raft of authorities that were cited by the parties drawn from the entire breadth of the Commonwealth where similar mechanisms exist, strongly suggest that the scheme is not unconstitutional and easily passes muster under ***Article 24*** of ***the Constitution***. (See ***Verimark Holdings Ltd v Brat Specialized Trustees (Pty) Ltd & 2 Others, Case No. 209/22928*** and ***Mtana Lewa v. Kahindi Ngala Mwagandi, CA No. 56 of 2014).***

As regards the chairman of the scheme creditors meeting, we note that after delivering the ruling of 31st July 2017 the learned judge heard the parties who wished to be heard, on the issue of the chairman of the scheme. He thereafter made an order which effectively modified the earlier order that had appointed Mr. Ngunze as the chairman and in his absence, Mr. Harney. The new order directed the creditors attending the first meeting of creditors to choose the chairman as the first item of business in the agenda. It is only in the absence of consensus within the first 30 minutes that Mr. Ngunze would chair the meeting and in his absence Mr. Harney would stand in for him. For our part, we are not persuaded that there is basis for interfering with that revised order by the High Court, taking into account the clear legal duties of the chairman, which he must discharge and be seen to discharge.

In our view, the main issue in this appeal is classification of the creditors as contemplated by ***section 923*** of the ***Act***, and more particularly whether, the unsecured creditors comprising commercial banks, that is the appellants and the 4th to 11th respondents should be in the same class as the 2nd respondent, which is

also a shareholder and guarantor of the 1st respondent.

In this regard the learned judge stated thus;

> ***"For now, I find that all the respondents belong to the class of unsecured lenders. It matters not the extent to which each has lent money to the petitioner. Some respondents have put in more than others, but the bottom-line is that all the respondents do not currently hold securities from the petitioner. If the petitioner were to go under, each of the creditors may end up losing the money which they advanced to the petitioner."***

The appellants' complaint is that not only is the 2nd respondent the single largest creditor of the 1st respondent, it is a director and the holder of a 29.8% shareholding of the 1st respondent. In addition, it is a guarantor to the scheme having issued a Sovereign Bond to secure the creditors. They contend that the 1st respondent's status and interest is in stark contrast to the rights and interests of the commercial banks which are regulated by the Central Bank, and who owe a responsibility and duty of care to their shareholders.

It is also the appellants' argument that as a consequence of the dissimilarities between themselves and the 2nd respondent, they should be in a separate class from the 2nd respondent and that a separate class meeting with the commercial banks should be convened.

In response, the 1st, 2nd and 4th to 11th respondents position is that there is no need for a separate class of creditors, comprising of only the commercial banks as, what is of essence in the classification of creditors is the rights and common interests of the parties.

Section 922 of the ***Companies Act 2015 Laws of Kenya*** expressly provides for compromises, arrangements and reconstruction. It states;

> ***(1) This Part applies when a compromise or arrangement is proposed –***
>
> ***(a) Between a company and its creditors, or any class of its creditors; or***
>
> ***(b) Between the company and its members, or any class of its creditors.***

No definition has been provided in the Act for the meaning of "class of creditors".

As to what constitutes a class was considered in the authoritative case of **Sovereign Assurance v Dodd (1892) (supra),** a case concerning a scheme of arrangement, where Bowen LJ said:

> ***"It seems plain that we must give such a meaning to the term class as will prevent the section being so worked as to result in confiscation and injustice, and that it must be confined to those persons whose rights are not so dissimilar as to make it impossible for them to consult together with a view to their common interest."***

The leading English authority on this issue is the Court of Appeal decision in ***Re Hawk Insurance Company Limited [2001] 2 BCLC*** which cited the Hong Kong case of ***Re UDL Holdings Limited [2002] 1 HKC 172*** where principles for ascertaining the composition of a class were set out as follows;

> ***"(2) Persons whose rights are so dissimilar that they cannot sensibly consult together with a view to their common interest must be given separate meetings. Persons whose rights are sufficiently similar that they can consult together with a view to their common interest should ne summoned to a single meeting***
>
> ***(3) The test is based on similarity or dissimilarity of legal rights against the company, not on similarity or dissimilarity of interests not derived from such legal rights. The fact that individuals***

might hold divergent views based on their private interests not derived from their legal rights against the company is not a ground for calling separate meetings.

(4) The question is whether the rights which are to be released or varied under the scheme or the new rights which the scheme gives in their place are so different that the scheme must be treated as a compromise or arrangement with more than one class."

And in the case of ***Re Telewest communications (No1) (supra)*** it was stated that;

"The approach to be adopted in the composition of classes for the purposes of s 425 has been the subject of a number of recent cases. Two issues in particular have been considered. First, the distinction between rights and interests has been underlined and it has been clearly reaffirmed that it is differences in rights, not interests that is relevant to the composition of classes. Secondly, the authorities have given important guidance as to the identification of relevant rights and the extent to which differences in rights require different classes."

As is evident from the above cited authorities, the general test for determining whether the members or creditors of a class should meet as a whole or in one or more separate classes is dependent on whether the rights of those concerned *"…are so dissimilar as to make it impossible for them to consult together with a view to their common interests…"*.

In the instant case, the appellants, and the 2nd to 12th respondents are all unsecured creditors of the 1st respondent and have been defined under the scheme as "Scheme Creditor". All have the same rights that have arisen by virtue of sums loaned to the 1st respondent, and their common interest is to recover these sums.

On the other hand, it is alleged that because the Government is also a shareholder and a guarantor it has dissimilar rights making it impossible for other creditors to consult with it. Going back to the test outlined in ***Re UDL Holdings Limited [2002] (supra),*** a class determination should be based on *"…similarity or dissimilarity of legal rights against the company, not on similarity or dissimilarity of interests not derived from such legal rights..."* The fact that government might hold other interests cannot be a basis for denying it the rights of an unsecured creditor, so as to necessitate the calling of separate meetings.

We are also of the view that the fact that a scheme creditor also holds a significant number of shares is not a basis for exclusion from the general class of unsecured creditors. (See ***Re Telewest communications (No1) (supra)*** and ***Buckley on the Companies Act, Butterworths, Twelfth Edition 1949***, page 157).

As to the ability to hold consultations, despite the appellants' contention that there have been no consultations, there is no evidence to show that they were locked out of consultations prior to the creditors' meeting, or did not have any opportunity to present their own proposals or express their views regarding the scheme. To the contrary, there is evidence of invitations to attend creditors meetings, exchange of emails amongst creditors and minutes of meetings held with creditors to discuss the various elements of the scheme. The fact of non attendance of the creditors meetings or refusal to engage in consultations by the appellants, or any other creditor for that matter does not in our view mean that consultations amongst creditors or with the 2nd respondent have been rendered impossible. We would therefore agree with the court below that *"…the assertion that the respondents could not consult together is wholly without foundation"*.

It is noteworthy that the 4th to 11th respondents who are also commercial banks are supportive of the scheme and have no objection to the current classification of creditors.

In view of our assessment of the material before us, we are not persuaded that the High Court erred as regards the classification of creditors or the appointment of chairman of the creditors meeting, and accordingly we have no reason to interfere with that decision. We have limited our determination specifically to the pertinent issues arising directly out of the impugned ruling of 31st July 2017. The other issues regarding the sanction of the scheme of arrangement as it has been presented by the 1st respondent

should be dealt with strictly as provided in the Companies Act. The consolidated appeals are dismissed with no orders as to the costs.

It is so ordered.

Dated and Delivered at Nairobi this 25th day August of 2017.

M. WARSAME

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JUDGE OF APPEAL

K. M'INOTI

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A. K. MURGOR

……..

JUDGE OF APPEAL

I certify that this is a true copy of the original

DEPUTY REGISTRAR