IN THE COURT OF APEAL

AT NAIROBI

(CORAM: MUSINGA, GATEMBU & M'INOTI JJ.A.

CIVIL APPEAL NO.272 OF 2006

BETWEEN

SAVINGS & LOAN (K) LIMITED.....APPELLANT

AND

KANYENJE KARANGAITA GAKOMBE.....1ST RESPONDENT

THE AUTOMOBILE ASSOCIATION OF KENYA....2ND RESPONDENT

(Appeal from the ruling and order of the High Court of Kenya at Nairobi (Ochieng J.) dated 3rd May 2006

in

H.C.C.C.No 1785 of 2000)

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JUDGMENT OF THE COURT

The central issue in this appeal is the vexed question whether a party who claims benefits under a contract to which he is not a party, can enforce that contract. A collateral issue in the appeal is whether a suit filed by such a party must invariably be struck out as disclosing no reasonable cause of action or as otherwise scandalous, frivolous and vexatious or an abuse of the court process. It is apposite to start by setting out the background tothe appeal before considering the issues raised therein.

By an agreement in writing dated 20th August 1997, the appellant, ***Savings & Loan Kenya Limited (S&L)*** and the 2ndrespondent, ***Automobile Association of Kenya (AA)*** entered into what was described as ***"Agreement to Administer AAK Members Home Loan Scheme"***. The recitals of the agreement stated that ***AA*** was desirous of extending financial assistance to its members to enable them acquire residential houses in Kenya. To that end ***S&L*** and ***AA*** had therefore designed, in a joint venture, a scheme to offer home loans at concessionary interest rates to members of ***AA (prospective buyers).*** To qualify for the scheme,prospective buyers were to maintain their membership with ***AA*** throughout the mortgage period. The purpose of the agreement was stated to be to formalize that arrangement between the ***S&L*** and ***AA*** and to operationalize the home loan scheme.

Other pertinent terms of the agreement were that themaximum amount available to prospective buyers

was Kshs 5 million; that the mortgage facility was restricted to purchase or construction of residential homes only; that ***AA*** would deposit 10% of the total subscription per annum into a House Deposit Account so as to boost the fund account; and that prospective buyers would save into the House Deposit Account 20% of the purchase price of their houses over 36 months by equal monthly instalments.

Finally it was agreed that upon satisfying the said conditions and meeting the ***S&L's*** lending requirements, ***S&L*** would advance a mortgage facility of 80% to the prospective buyers to complete the purchase of their houses. Regarding repayment, it was agreed that the loan would be repaid over the agreed period and interest would be charged at a concessionary rate of 8% per annum on monthly reducing balances.

By clause 14 of the agreement, the parties agreed that either party could terminate the loan scheme by giving the other three months notice of its intention to do so.

As is patently clear, the agreement of 20th August 1997 provided for ***S&L*** to finance the purchase or construction of residential houses by ***AA's*** members. The agreement did not address the case of ***AA's*** members who had existing mortgages with other financiers. By its brochure entitled ***"AAK MEMBERS HOME LOAN SCHEME"*** which was meant to publicize the scheme, ***S&L*** highlighted the terms and conditions of the home loan scheme that we have set out above. That brochure stated that three types of home loans, namely, (i) first time home buyers, (ii) upgrading and (iii) refinancing, were available to AA's members under the scheme. Of relevance to this appeal is the third type of loan (refinancing) in respect of which the brochure provided as follows:

> ***"Where members are servicing home loans with other financial institutions, the facility can be transferred to the AAK Home Loan Scheme, provided that the member can save 10% of the outstanding loan, over a period of 24 months, and the existing loan has been regularly serviced."***

It is worth noting that while the homebuyers under the agreement were to save 20% of the purchase price by 36 equal monthly instalments, according to the brochure AA's members who already had mortgages with other financial institutions were required to save 10% of the outstanding loan over a period of 24 months.

The 1st respondent, ***Dr. Kanyenje Karangaita Gakombe(Dr. Gakombe)*** was at the material time a life member of ***AA*** and held a loan with a financial institution called ***Co-Trust Investments Ltd***. Taking advantage of the refinancing loan, he opened a ***House Deposit Account No. 109002242*** with ***S&L*** and applied for refinancing which was accepted by S&L. He subsequently opened a separate mortgage account ***No. 109005919*** with ***S&L*** into which he deposited funds for mortgage approval fees, valuation, and other miscellaneous expenses. Ultimately he saved with ***S&L*** 10% of the value of his existing loan with ***Co-Trust Investments Ltd*** for a period of 24 months and at the same time continued serving his loan with ***Co-Trust Investments Ltd,*** as required. ***S&L*** later organized for the valuation of his property by a firm known as Landmark Realtors.

In the meantime the mortgage scheme ran into problems, and invoking clause 14 of the agreement, ***S&L*** terminated the agreement by a letter dated 22nd February 2000.

After failing to get the refinancing facility from ***S&L,*** on 6th October 2000, Dr. Gakombe filed ***HCCC No. 1785 of 2000*** against both ***AA*** and ***S&L***, seeking among others, an order compelling ***AA*** & ***S&L*** to extend to him a mortgage facility at 8% p.a. conscetionary rate, damages for loss of earnings on the moneys deposited with ***S&L*** and general damages. As pleaded in the plaint, Dr. Gakombe's claim was founded on refinancing, it being alleged that ***AA*** had offered a refinancing facility to its existing members, which, as one such member, he had accepted and opened the requisite deposit account with ***S&L***. It was alleged that after complying with all the conditions ***AA*** and ***S&L*** had breached the agreement.

In its defence dated 3rd November 2000, ***S&L*** averred that Dr. Gakombe was required to save 20% of the

purchase price over a maximum period of 36 months by equal monthly instalments. It was further pleaded that ***S&L*** terminated the agreement between itself and ***AA*** on account of breach of the agreement by ***AA***.

For its part, ***AA***, in its defence dated 13th November 2000, denied the existence of any agreement between itself and Dr. Gakombe regarding the mortgage facility. While admitting the existence of the agreement of 20th August 2000, ***AA*** pleaded that it had no say on how any of its members were to enter into contracts with ***S&L***.

On 26th July 2005, ***S&L*** applied under the then ***Order VI Rule 13 (b) (c) and (d)*** of the ***Civil Procedure Rules*** to strike out the suit as against itself, on the basis that it offended the doctrine of privity of contract. It was contended that Dr. Gakombe's suit was founded upon an agreement to which he was not a party and to that extent the suit was scandalous, frivolous and vexatious. In addition it was argued that the agreement between ***S&L*** and ***AA,*** having been terminated by the former vide the letter dated 22nd February 2000, the same ceased to have effect after three months by virtue of clause 14, yet Dr.Gakombe's suit was filed October 2000, long after the effective termination of the agreement.

Both Dr. Gakombe and ***AA,*** resisted the application, the former arguing that he had entered into a separate agreement with **S&L** regarding refinancing. That view was shared and supported by ***AA***.

The application was heard by ***Ochieng, J***. who in a considered ruling, dismissed the same with costs after holding that while the agreement dated 20th August 2000 was between ***S&L*** and ***AA*** and could not therefore, on account of privity of contract, be enforced by Dr. Gakombe, nevertheless Dr. Gakombe's contention that there was a separate contract between him and S&L was not idle and could not be dismissed off-hand.

Aggrieved by the ruling, S&L lodged a notice of appeal and subsequently applied successfully for stay of further proceedings in the High Court pending the hearing and determination of its interlocutory appeal.

Before us, ***Mr. Karori,*** learned counsel for ***S&L*** assailed the ruling of the High Court on the ground that it had ignored the doctrine of privity of contract. It was submitted that the agreement upon which Dr. Gakombe's suit was based was between ***S&L*** and ***AA*** to the exclusion of Dr. Gakombe, yet this non-party was seeking specific performance of that agreement. It was also contended that in any event, ***S&L*** had, after breach by **AA**, effectively terminated the agreement pursuant to ***clause 14,*** long before Dr. Gakombe filed his suit.

Learned counsel challenged the view that there existed a separate contract between ***S&L*** and Dr. Gakombe. He contended that no such agreement had been produced and that in any event its terms were contrary to the agreement between ***S&L*** and ***AA***. In Mr. Karori's view, the opening of an account by Dr.Gakombe in ***S&L*** was in furtherance of the agreement between ***S&L*** and ***AA*** and did not constitute evidence of an independent contract between ***S&L*** and Dr. Gakombe.

Relying on the judgments of this Court in ***AGRICULTURAL FINANCE CORPORATION V LENGETIA LTD [1985] KLR 765, KENYA NATIONAL CAPITAL CORPORATION LTD V ALBERT MARIO CORDEIRO & ANOTHER, CA NO 274 OF 2003*** and ***WILLIAM MUTHEE MUTHAMI V BANK OF BARODA, CA NO 91 OF 2004***, Mr. Karori submitted that a contract affects only the parties to it and that it cannot be enforced by or against a non party. Accordingly we were urged to allow the appeal, set aside the ruling of the High Court and substitute therefore an order allowing ***S&L's*** application for striking out of Dr. Gakombe's suit with costs.

Mr. Mari, learned counsel for Dr. Gakombe and ***Mr. Nyaencha,*** learned counsel for ***AA,*** opposed the appeal. Mr. Mari defended the ruling of the High Court for finding that the suit disclosed triable issues, which could not be determined without a full hearing. The appellant was criticized for seeking to determine disputed issues on the basis of affidavit evidence without the benefit of a hearing entailing examination and cross-examination of the parties. Leaned counsel contended that the agreement between ***S&L*** and ***AA*** was explicit enough that it was for the benefit of ***AA's*** members like Dr. Gakombe and in

those circumstances, a member of ***AA*** who was intended by ***S&L*** and ***AA*** to benefit from the agreement could lawfully enforce it. As regards the refinancing facility, Mr. Mari contended that it was a collateral agreement between ***S&L*** and Dr. Gakombe.

Mr. Nyaencha adopted the submissions made on behalf of Dr. Gakombe, in particular supporting the view that where an agreement is intended for the benefit of a third party, an exception to the privity of contract doctrine arises, thus making it possible for the third party to enforce the agreement. In his view, the best option was to allow the suit in the High Court to proceed to hearing to enable the court determine all the issues raised by the parties.

We have carefully considered the ruling of the High Court, the grounds of appeal, the submissions of respective counsel, the authorities cited and the law.

In its classical rendering, the doctrine of privity of contract postulates that a contract cannot confer rights or impose obligations on any person other than the parties to the contract. Accordingly a contract cannot be enforced either by or against a third party. In ***DUNLOP PNEUMATIC TYRE CO LTD V SELFRIDGE & CO LTD [1915] AC 847,Lord Haldane, LC*** rendered the principle thus:

> ***"My Lords, in the law of England certain principles are fundamental. One is that only a person who is a party to a contract can sue on it."***

In this jurisdiction that proposition has been affirmed in a line of decisions of this Court, among them ***AGRICULTURAL FINANCE CORPORATION V LENGETIA LTD (supra), KENYA NATIONAL CAPITAL CORPORATION LTD V ALBERT MARIO CORDEIRO & ANOTHER (supra)*** and ***WILLIAM MUTHEE MUTHAMI V BANK OF BARODA, (supra).***

Thus in ***AGRICULTURAL FINANCE CORPORATION V LENGETIA LTD (supra)***, quoting with approval from ***Halsbury's Laws of England, 3rd Edition, Volume 8, paragraph 110***, ***Hancox, JA,*** as he then was, reiterated:

> ***"As a general rule a contract affects only the parties to it, it cannot be enforced by or against a person who is not a party, even if the contract is made for his benefit and purports to give him the right to sue or to make him liable upon it. The fact that a person who is a stranger to the consideration of a contract stands in such near relationship to the party from whom the consideration proceeds that he may be considered a party to the consideration does not entitle him to sue upon the contract."***

Over time some exceptions to the doctrine of privity of contract have been recognized and accepted. Among these exceptions is where a contract between two parties is accompanied by a collateral contract between one of them and a third party relating to the same subject matter. Thus in ***SHANKLIN PIER V DETEL PRODUCTS LTD [1951] 2 KB 854,*** for example, the plaintiff owned a pier, which it wished to be repainted. After the defendant represented to the plaintiff that some particular paint was fit for purpose, the plaintiff directed its contractor to use that paint. The contractor purchased the paint from the defendant, which proved unfit for purpose. Upon a suit by the plaintiff against the defendant, the court found for the plaintiff notwithstanding the fact that there was no privity of contract between the plaintiff and the defendant, as far as the contract for the sale of the paint was concerned.

While the proposition that a contract cannot impose liabilities on a non-party has been widely embraced and accepted as rational and well founded, the proposition that a contract cannot confer a benefit other than to a party to it has not been readily accepted and has in fact been the been subject of much criticism. In ***DARLINGTON BOUROUGH COUNCIL V WITSHIRE NORTHERN LTD [1995] 1 WLR 68 Lord Steyn*** eloquently demonstrated the flaw in the proposition in the following terms:

> ***"The case for recognizing a contract for the benefit of a third party is simple and straightforward. The autonomy of the will of the parties should be respected. The law of contract should give effect to the reasonable expectations of contracting parties. Principle certainly***

requires that a burden should not be imposed on a third party without his consent. But there is no doctrinal, logical or policy reason why the law should deny effectiveness to a contract for the benefit of a third party where that is the expressed intention of the parties. Moreover, often the parties, and particularly third parties, organize their affairs on the faith of the contract. They rely on the contract. It is therefore unjust to deny effectiveness to such a contract."

Some jurisdictions have, accordingly and in a bid to introduce reforms and ameliorate the harshness of the rule,resorted to legislative intervention. The best examples are the United Kingdom and Singapore where the ***Contracts (Rights of Third Parties) Act, 1999*** and the ***Contract (Rights of Third Parties) Act, 2001*** have respectively been enacted.

Back to the appeal before us, it is a hotly contested issue whether in addition to the contract between ***S&L*** and ***AA*** for the benefit of the latter's members, there was also a collateral agreement between ***S&L*** and Dr. Gakombe regarding the same subject matter.

The agreement dated 20th August 1997 between ***S&L*** and ***AA*** provided for financing the purchase or construction of homes for members of ***AA***. The prospective buyers were required to save 20% of the purchase price over 36 months by equal monthly instalments. Dr. Gakombe's claim is founded on refinancing of existing loans, which *prima facie* appears to be based on different terms from those set out in the agreement between ***S&L*** and ***AA***. The terms of the refinancing, unlike those set out in the agreement between ***S&L*** and ***AA*** involved saving 20% of the outstanding loan over a period of 24 months.

In these circumstances, can Dr. Gakombe's suit be described as one, which discloses no reasonable cause of action because of the doctrine of privity of contract, or a suit which is scandalous, frivolous and vexatious? In our view, the learned judge was justified in concluding that Dr. Gakombe's contention that there was a collateral agreement between him and ***S&L*** on refinancing was not idle and that his suit did raise triable issues, which deserved to be interrogated and determined only after a full hearing of the suit. On this issue, we shall not say more because, as this Court has consistently stated, it is inadvisable, in an interlocutory appeal, to express any concluded views on matters that are pending trial. The basis of that approach is to avoid prejudicing any of the parties. (See ***BP (KENYA) LTD V. KISUMU MARKET SERVICE STATION, CA No. 25 of 1992*** and ***DAVID KAMAU GAKURU V. NATIONAL INDUSTRIAL CREDIT BANK LTD, CA No. 84 of 2001)***.

We conclude therefore that Dr. Gakombe's suit raises *bona fide* issues worth of consideration and that it is for the trial court to determine, after full hearing of the suit, whether Dr. Gakombe's suit is caught by the doctrine of privity of contract or whether he had an enforceable collateral agreement with ***S&L***, among any other issues that the parties and the trial courts may frame for determination.

This Court has, in addition, consistently held that the power to strike out a suit as one disclosing no reasonable cause of action is a drastic power, which should be exercised sparingly, and only in plain and obvious where the Court has no doubt that the plaintiff has no case at all. In ***DT DOBIE CO LTD V MUCHINA [1982] KLR 1, at page 9***, ***Madan JA***, as he then was, stated as follows:

"No suit ought to be summarily dismissed unless it appears so hopeless that it plainly and obviously discloses no reasonable cause of action and is so week as to be beyond redemption and incurable by amendment. If a suit shows a mere semblance of a cause of action, provided it can be injected with real life by amendment, it ought to be allowed to go forward for a court of justice ought not to act in darkness without the full facts of a case before it."

And in ***CORPORATE INSURANCE CO LTD V NYALI BEACH HOTEL LTD CA NO 270 OF 1996, Gicheru, JA***, as he then was, warned that summary procedure, like the striking out of suits, should not be allowed to become a means of avoiding a trial and obtaining immediate judgment. That in our view still underlines the view that this procedure should not be resorted to, save in the clearest of cases.

Ultimately therefore, we have concluded that Dr. Gakombe's suit does not fall in the category of suits that

may be described as “plainly and obviously disclosing no reasonable cause of action” and that the High Court did not err by refusing to strike it out. This appeal therefore is bereft of merit and is accordingly dismissed with costs to the respondents. It is so ordered.

Dated and delivered at Nairobi this 24th day of April 2015.

D. K. MUSINGA

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JUDGE OF APPEAL

S. GATEMBU KAIRU

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JUDGE OF APPEAL

K. M’INOTI

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JUDGE OF APPEAL

I certify that this is a true copy of the original

DEPUTY REGISTRAR