**Karmali and another v CFC Bank Limited and another**

**Division:** Milimani Commercial Court of Kenya at Nairobi

**Date of judgment:** 2 May 2006

**Case Number:** 3/06

**Before:** Ochieng J

**Sourced by:** LawAfrica

**Summarised by:** E Ongoya

*[1] Charges and mortgages – Distinction between charges and mortgages – Variation of interest*

*clauses – Whether such clauses render a charge void – Undue influence and coercion against surety –*

*Whether husband and wife relation can raise presumption of undue influence.*

**RULING**

**Ochieng J:** On 10 January 2006 the two plaintiffs filed a plaint instituting the suit herein. Simultaneously with the plaint, the plaintiffs filed a Chamber Summons through which they sought interlocutory injunctive reliefs. It is the plaintiff’s case that no statutory power of sale can arise from the charge registered against the suit property because the said property was given to them as a wedding present. The second plaintiff, in particular, is said to have a sentimental attachment to the property. I must say that when the advocate for the plaintiffs had made those initial statements, I wondered to myself if the court was in for a new and previously unchattered line of submissions. Indeed, I said to myself, at that point in time, that if a security could not be sold off by a chargee on the grounds that the chargor was sentimentally attached to it, by virtue of the manner in which he had acquired ownership thereto, then chargees would find it impossible to exercise their statutory powers of sale. But, I should not have had reason to habour any of those thoughts. Soon enough, it became clear to me that this was a battle of titanic proportions. No, it is not simply because the suit property had been given to the plaintiffs as a wedding gift that they believed gave rise to the need for the property to be safeguarded by an injunction. The real reason emerged to be the assertion that the second defendant was coerced to execute the charge document. It was the second defendant’s case that her husband, who is the first defendant herein, caused her to execute the charge document so as to secure some debt which Hyundai Motors Limited owed to the first defendant. In order to understand the alleged coercion, it is necessary to place facts within perspective. Firstly, it was a fact that the first plaintiff, Mohamed Gulamhussein Farzal Karmali, was a director of Hyundai Motors Limited. In turn, that company was said to be indebted to the first defendant to the tune of KShs 80 million. In those circumstances, the first defendant is said to have exerted pressure on Hyundai Motors Limited to pay the debt. Being a director and a shareholder of 30% of the shares in Hyundai Motors Limited, the first defendant was personally under pressure, from both his fellow directors as well as from the first defendant. On the second plaintiff’s part, she says that her husband had informed her: “That the said first defendant was now putting pressure on the board of directors to service the facility and he had been personally asked to charge/mortgage our residential house (Land Reference number 3734/1168) for KShs 10 500 000 for the proceeds thereto to be credit (*sic*) in the Hyundai Motors (K) Limited account.” It is her case that she resisted the idea of offering the suit property as security. However: “Due to the bank’s bigger bargaining power coerced the first plaintiff and myself to concede to charge our house to them due to the representation that Hyundai Motors (K) Limited was heavily indebted and the bank threatened to pursue the company itself by either winding it up, or appoint a receiver or in any other way exercise its contractual rights to recover the said money.” Those circumstances do explain, from the plaintiffs’ perspective, how they came to the stage of executing a legal charge in favour of the first defendant, to secure the indebtedness of Hyundai Motors (K) Limited. And, it later transpired that Hyundai Motors (K) Limited (Hereinafter cited as Hyundai Motors) did not owe money to the first defendant, say the plaintiffs. That could therefore only imply that the first defendant had exercised undue duress and coercion on the plaintiffs, so it was submitted. Relying on the treatise “Chitty on Contracts”, the plaintiffs submitted that if the court found that there had been duress that would imply that there was an absence of contract. And, in this case wherein a fiduciary relationship was said to have been in existence, as between the plaintiffs themselves, and also as between the plaintiffs and the bank, the plaintiffs assert that they have proved they had signed the charge document under duress. That fact would, in the plaintiff’s mind, render the charge voidable, at their instance, as they were the victims of the first defendant’s duress. The second point taken up by the plaintiffs was that no statutory powers of sale could arise herein, on the basis of section 46 of the Registration of Titles Act (Chapter 281). That section is said to make it mandatory for all charge documents to conform to the requirements of either form J(1) or J(2). The charge here is said to provide for interest other than simple interest, as envisaged in forms J(1) and J(2). Therefore, the plaintiff contends that the charge derogates from section 46, and thus ceases to be a charge which can borrow from section 100 of the Registration of Titles Act. For that reason, the plaintiff submits that the document described as a charge herein could not give to the chargee any power of sale. The charge is further faulted for not having an amortisation clause as required by statute. That is because the charge allows penalties, which therefore makes amortisation impossible as the repayment period was effectively varied through the provisions which allowed for variation of interest rates. The other issue which was canvassed by the plaintiff was in relation to the provisions of section 39(1) of the Central Bank of Kenya Act 4 of 2001. That section pegs interest chargeable by mortgagees to the 91–day Treasury Bill rates. As Act 4 of 2001 came into force on 1 January 2001, whilst the loan herein was given out on 8 April 2002, the plaintiffs submit that the maximum sum which the defendant could recover was KShs 21 million, which sum is equivalent to double the loan sum of KShs 10 500 000. In the circumstances, the plaintiffs believe that any demand for sums in excess of KShs 21 million was unlawful, by virtue of the maximum recovery allowed by statute. Another issue raised by the plaintiff was to the effect that the defendant had so mixed up the loan accounts of the plaintiffs with the account of Hyundai Motors Kenya Limited, that the sum which was loaned to the plaintiffs was incapable of identification. Thereafter, on 10 August 2004, the defendant is said to have written-off the sum of KShs 96 065 606. Therefore, the plaintiffs say that they have no obligation to pay the sums which were lumped together with those of Hyundai Motors. In any event, the defendant was charging penalties which were in excess of two years old, and that was contrary to section 4 of the Limitation of Actions Act, said the plaintiffs. That was yet one more reason why the plaintiffs feel that they should not be compelled to pay the sums claimed by the defendant. For all those reasons, the plaintiffs submitted that they were entitled to an order pursuant to section 52 of the Indian Transfer of Property Act, prohibiting any registration of change of ownership of the property from the plaintiffs. The court was therefore asked to grant the prayers sought in the application. When responding to the application, the defendant first submitted that the tests which the plaintiffs were obliged to meet if they were to get any of the injunctive reliefs sought were those set out in *Giella v Cassman Brown and Company Limited* [1973] EA 358. Of course, that celebrated decision remains the beacon for determination of applications for interlocutory injunctive reliefs. In other words, the applicant must first prove a *prima facie* case with a probability of success. Secondly, an interlocutory injunction will not normally be granted unless the applicant might otherwise suffer irreparable injury which could not be adequately compensated in damages; and thirdly, if the court is in doubt, it will decide the application on a balance of convenience. Bearing those principles in mind, the defendant submitted that the plaintiffs’ assertions on the alleged invalidity of the charge instrument was no more than an expression of the plaintiffs’ confusion. The said confusion is attributed to the “fact” that the plaintiffs had mixed up the provisions governing charges with those governing mortgages. Just to be sure that the distinction between the two is clear, it is to be noted that section 58(*d*) of the Transfer of Property Act defines a mortgage, as follows: “A mortgage is the transfer of an interest in specific immovable property for the purpose of securing the payment of money advanced or to be advanced by way of loan, an existing or future debt, or the performance of an engagement which may give rise to a pecuniary liability.” The significant feature of a mortgage is thus the transfer of an interest in specific immovable property. In contrast, section 100 of Transfer of Property Act defines a charge, as follows: “Where immovable property of one person is by act of the parties or operation of law made security for the payment of money to another, and the transaction does not amount to a mortgage, the latter person is said to have a charge on the property; and all the provisions hereinbefore contained as to a mortgagor shall, so far as may be, apply to the owner of such property, and the provisions of sections 81 and 82 and all the provisions hereinbefore contained as to a mortgagee instituting a suit for the sale of the mortgaged property shall so far as may be, apply to the person having such charge.” In this case the suit property is registered under the Registration of Titles Act. Under that statute the only form of security is a charge. There is absolutely no mention of mortgages in the Registration of Titles Act. Therefore, I believe that a mortgage could not be created under that statute. It thus follows that the security herein, is, as it describes itself on the face of the document, a charge. It is common ground that pursuant to the provisions of section 46(1) of the Registration of Titles Act, a charge ought to be executed in form J(1) or J(2) in the first schedule. However, section 46 does not stipulate the manner in which the charge document is to be attested. To my mind, one must then fall back on the provisions of section 69(4) of the Transfer of Property Act to ascertain how the charge document is to be attested. The said section makes it clear that the statutory powers of sale would only accrue: “If the mortgagor’s signature to the mortgage instrument has been witnessed by an advocate and if the said instrument bears a certificate signed by that advocate to the effect that he has explained to the mortgagor the effect of subsection (1) of this section and he was satisfied that the mortgagor understood the same.” Whereas that section makes reference to mortgage instruments and mortgagor’s statutory power of sale, one must not lose sight of section 100A which expressly equates the rights, powers and remedies of a chargee to those of a mortgagee. But then, the plaintiffs have noted that whereas the charge instrument is said to be a charge, the contents thereof make reference to “mortgagors” throughout. Whilst that is the position, the plaintiffs did not suggest that by making references to “mortgagors” within the body of the charge instrument, that alone would render the security void or voidable. Of course, such reference reflects confusion on the part of the defendant, who had expressed a keen sense of distinction between a charge and a mortgage. Speaking for myself, I do not think that by making reference to “mortgagor” instead of “chargor” would, by itself invalidate the charge instrument. But that still begs the question whether or not the charge document was void for allegedly failing to comply with the provisions of section 46(1) of the Registration of Titles Act, insofar as that section requires that a charge be either in form J(1) or form J(2). In that regard, the plaintiff cited *Kenya Commercial Finance Company Limited v Ngeny and another* [2002] 1 KLR 106, as authority to support their contention. At 126 of the law report, Lakha JA expressed himself thus: “It is mandatory that the charge shall be executed in form J(1) or J(2) in the First Schedule which in turn requires the rate of interest to be specifically stated. The charge in the instant case omits to state the rate of interest rendering the charge defective.” Firstly, the defendant pointed out that the decision of Lakha JA was a dissenting judgement. That is an undisputed fact. But, the plaintiffs say that on that point of law, the other two judges did not express a different opinion, and that therefore the holding by Lakha JA was good law in that regard. Having carefully perused the other two judgements, I accept the plaintiff’s observation, to the effect that they did not specifically address the provisions of section 46(1) of the Registration of Titles Act. For that reason, the pronouncement by Lakha JA cannot be disregarded simply because his was a dissenting judgement. But I still ask myself if that necessarily implies that it is good law. The defendant purported to provide an answer to that question by citing the decision in *Fina Bank Limited v Ronak Limited* [2001] EA 54. In that case it had been argued by the chargor that the charge was unenforceable on the grounds that no interest rate was stipulated in the charge document; that variation of interest rates was unenforceable; and that the said rates were onerous and oppressive. The Court of Appeal unanimously upset the injunction which the Superior Court had granted, as it found nothing wrong with the variation of interest rates, or with the fact that no exact rate or rates had been specified. In arriving at its decision, the Superior Court had said: “Upon perusal of the charge documents which form part of the exhibits that were attached to the replying affidavit, it is evident that although the bank reserved the right to vary the rate of interest, there was, however, no rate specified therein as either the base lending rate, minimum rate, or the commencing rate of interest for the facility. Had the rate been specified, then, I would have had no difficulty in finding in favour of the bank. As the matter now stands, the agreement which forms the basis for the contractual relationship between the parties hereto is silent on that particular issue, in which event the rate cannot be inferred by the court.” From my understanding of the foregoing, the Superior Court had not directly addressed the issue of section 46(1) of the Registration of Titles Act. Indeed, neither the Superior Court nor the Court of Appeal mentioned either that statutory provision or even forms J(1) and J(2), in their respective judgements. Therefore, even though the bottom-line of the decision by the Court of Appeal appears to support the defendant’s position in this case, it is not explicit. On my part, I hold the considered view that provided parties to an instrument of charge have a clear agreement on the interest which is to be charged on the facility, it would not matter if the rate is variable. That is what I understand their Lordships to have determined in *Fina Bank Limited v Ronak Limited* (*supra*). By implication, it would mean that a charge instrument which provided for variable interest would not be void or voidable simply because it did not specify one rate of interest, or a specified instalment amount. If one were to hold that instruments of charge would only be valid if they specified one rate of interest, as well as a specified instalment amount, he would have become so unrealistic as to be limiting parties’ freedom of negotiation. Form J(2) does readily recognise the fact that parties can agree on such matters as: “The times appointed for the payment of the sum; annuity; rent charge intended to be secured; *the interest if any*; and the events on which such sum, annuity or rent charge shall become and cease to be payable; *also any special agreement or powers*.” [Emphasis mine.] In the circumstances, I hold that the charge instrument herein is not void, as alleged by the plaintiffs. In my considered opinion, when parties to a charge instrument agree that the chargee may vary the rate of interest, and the said agreement is incorporated into the instrument, that does not amount to a deviation from the forms provided in the schedule to the Registration of Titles Act. As I have already said, form J(2) actually allows the parties to agree on interest, if any. In other words, a chargee is not compelled, by statute, to charge a fixed interest on the facility it may accord to the chargor. If the chargee should agree with chargor that interest would be payable, the parties need only incorporate such an agreement into the instrument of charge. The next issue which the defendants delved into was in relation to what is perceived by them as constituting material non-disclosure, on the plaintiffs’ part. The submissions in that regard are said to be founded upon matters which the plaintiff had asserted, but which the defendants later disproved. The matters are as follows: (*a*) Attestation of the instrument of charge. (*b*) Service of a statutory notice. (*c*) Section 3(3) of the Law of Contract Act. Attestation of Charge The plaintiffs had asserted that the instrument was attested by an advocate who did not hold a practising certificate at the material time. When the defendants adduced proof to counter the assertion that Naheed-Kadernani did not hold a valid practising certificate at the time in question, the plaintiffs conceded the point. Statutory Notice The plaintiffs had stated, under oath that the first defendant had not served a statutory notice. In response, the first defendant made available proof of service, whereupon the plaintiff conceded the point. Law of Contract Act The plaintiffs asserted that the charge infringed the provisions of section 3(3) of the Law of Contract Act. That section provides as follows: “No suit shall be brought upon a contract for the disposition of an interest in land unless: (*a*) the contract upon which the suit is founded: (i) is in writing; (ii) is signed by all the parties thereto; and (b) the signature of each party signing has been attested by a witness who is present when the contract was signed by such party. Provided that this subsection shall not apply to a contract made in the course of a public auction by an auctioneer within the meaning of the Auctioneer’s Act, nor shall anything in it affect, the creation of a resulting, implied or constructive trust.” In my reading of the application and the affidavit in support thereto, I did not get to fully appreciate the particular shortcoming complained of by the plaintiffs. But, in any event, the plaintiffs did concede that the issue was not worth pursuing. The significant issue in that regard was the timing of the concessions on the three points. The concessions were not made at the outset, when the plaintiffs commenced prosecuting the application. Also, the concessions were not made during the submissions by the plaintiffs, advocates. Instead, the concessions were made when the advocate for the defendants was about to delve into each one of the three points above. In the light of the timing of the concessions, the defendant submitted that the plaintiffs ought to be deemed as being guilty of material non-disclosure. The court was invited to hold that for that reason, the plaintiffs were undeserving of the equitable remedy of an injunction. Having given due consideration to the competing submissions made by the parties herein, I am unable to share the defendant’s viewpoint. I say so, not because I do not appreciate the defendants’ feeling, that the plaintiffs were trying everything possible to get an injunction. True, I agree that if any party has made an assertion which has then been controverted by the other party, it is a sign of good practice to make concessions at the earliest opportunity. Indeed, before any party makes assertions such as may suggest that an advocate did not have the requisite practising certificate, it is vital that the party cross-checks his facts with the relevant authority, such as the Law Society of Kenya. Indeed, prudence may dictate that the advocate be asked to confirm the information, so as to avoid the possibility of soiling the reputation of persons who were compliant. On the other hand, I appreciate that in litigation, there will be moments where parties may not have sufficient time and opportunity to cross-check facts. In such instances, it is best that the allegations are not made at all. As regards an assertion that no statutory notice had been served, I am unable to understand how the chargor can justify the same. A chargor who says that no such notice had been served, whilst he had actually been served, is walking a very thin line between oversight and non-disclosure. But, as regards the citation of statutory provisions, I hold the view that it does not amount to non-disclosure if the party is shown to have been wrong. In conclusion, the main reason why the three points herein were not held as amounting to non-disclosure is the fact that the plaintiffs did not purport to canvass any of them, when prosecuting the application herein. I am aware that by that time, the assertions may well have influenced the court, at the stage when the application first came up before the court, but in this case, the plaintiffs did not strive to steal a march on the defendants, by seeking *ex parte* orders in the first instance. Had the plaintiffs sought *ex parte* orders, in the first place, they may well have been held to have been guilty of material non-disclosure. In that event, the court may have had to determine whether or not it would have been sufficient to discharge such *ex parte* orders as may have been obtained, or whether the case was one which called for the more serious step of refusing to give a further hearing to the merits of the plaintiff’s application. The next point was in relation to The Banking (Amendment) Bill 2004. That Bill was published in the special issue of the Kenya Gazette Supplement dated 10 June 2004. The Bill seeks to amend The Banking Act, by introducing section 44A, so as to limit the total interest an institution can recover on a non-performing loan. The intention is to limit the interest to the amount of the outstanding principal amount, at the time the loan became non-performing. And, for loans which became non-performing before the proposed amendment came into operation, the additional interest is not supposed to exceed the total principal and interest owing at the time the section comes into operation. The court was not satisfied that the Bill has yet been passed by parliament. Therefore, I am unable to apply it. Indeed, when the plaintiffs were faced with the question as to when the said Bill became law, I understood them to be unsure, and therefore they only reemphasised the provisions of section 39 of Act 4 of 2001. There is no doubt that the said Act, which is otherwise known as the Central Bank of Kenya (Amendment) Act of 2000, came into force on 1 January 2001. Section 39(1) of the Act stipulates as follows: “The maximum rate of interest which specified financial institutions may charge on loans or advances shall be the 91 – day Treasury Bill rate published by the Bank on the last Friday of each month, or the latest published 91 – day Treasury Bill rate, plus four *per centum*: Provided that the maximum interest chargeable under this subsection shall not exceed the principal sum loaned or advanced and provided further that this subsection shall only apply to contracts for loans or advances made or renewed after the commencement of this section.” The loan or advances in issue were said to have been given on 8 April 2002. Therefore the said facility would be subject to the provisions of section 39(1) of the Central Bank of Kenya Act. As the facility was for KShs 10 500 000 the plaintiffs submitted that the first defendant was not entitled to demand anything more than KShs 21 million. Yet, by a letter dated 24 October 2005, the first defendant demanded payment of KShs 21 289 324,85. To my mind, that demand raises a very serious issue, as the sum sought was in excess of double the amount which was secured by the charge executed by the plaintiffs. That would imply that the interest charged was probably in excess of the principal loan amount. In the circumstances, until and unless the first defendant was able to demonstrate that the interest charged did not exceed the principal amount loaned or advanced, I find that the plaintiffs have established a *prima facie* case with a probability of success. Another issue which has caused me considerable concern relates to the alleged duress and coercion which was said to have been exerted on the plaintiffs. The coercion is said to have taken the form of a threat to wind-up Hyundai Motors Kenya Limited. To my mind, if a creditor should issue a lawful demand, which is intended to lead to the recovery of a debt through a recognised court process, the creditor cannot be accused of duress or coercion. Thus, a creditor would be perfectly entitled to give notice of intention to commence winding-up proceedings against a company which was indebted to him. The creditor would, similarly, be entitled to give notice of his intention to commence bankruptcy proceedings against an individual who owed him money. Such demands should not be construed as duress or coercion. But, the plaintiffs are saying that the demands themselves were without foundation, as the creditor, Hyundai Motors Kenya Limited did not owe the money which the first defendant was seeking to recover. The reason for the plaintiffs’ belief that Hyundai Motors did not owe the money, was the fact that on 10 August 2004, the first defendant wrote-off the sum of KShs 96 065 606, as a bad debt. In my understanding a “Bad debt write-off” does not connote the absence of a legitimate claim against the debtor whose debt is being written-off. A creditor would write-off a bad debt as a process of updating his records, once he came to the conclusion that the prospects of recovering the debt were literally non-existent. Therefore, I am unable to accept the plaintiffs’ contention, to the effect that simply because the first defendant decided to write-off the debits in the account of Hyundai Motors as a bad debt, the said company had not been indebted to them. However, that still begs the question as to whether or not there had been duress or coercion. The second plaintiff deponed that she had resisted the attempts by the first plaintiff to offer the suit property as security for the facility accorded to Hyundai Motors. Notably, the second plaintiff has not alluded to any duress or coercion flowing directly from the first defendant, directed at her personally. In giving due consideration to this aspect of the application, I first remind myself of the following words of Ringera J (as he then was) in *Simiyu v Housing Finance Company of Kenya Limited* [2001] 2 EA 540 at 546: “In answering that question the court is to remember that it is not required - indeed it is forbidden – to make definitive findings of fact or law at the interlocutory stage particularly where the affidavits are contradictory and the legal propositions are hotly contested as is the case here.” I have felt the need to so remind myself, because there can be no doubt about how hotly contested this matter has been. In *Ottoman Bank v KS Mawani and others* [1965] EA 464 at 465, Rudd J held as follows: “He was told by the plaintiff’s assistant manager that he should sign but I do not find any undue influence on the part of the plaintiff bank. The question is whether his father exercised undue influence on the third party defendant to sign and if so, whether the court should absolve the third defendant from liability on that account.” Thereafter, the court analysed the evidence on record and came to the conclusion as follows, at 466: “On the whole I consider that there is just enough here to sustain the defence of undue influence and not enough to rebut the presumption that arises from the third defendant’s known filial relationship to his father and his subservience to him in affairs of the business which ought to have been sufficiently noticeable, to put the plaintiffs on their guard. No steps at all appear to have been taken to see that the third defendant acted as a free agent with knowledge of the full probable effects on him of his guarantee.” Whilst the first defendant herein has said that it did take steps to ensure that the second plaintiff obtained independent legal advise, the said plaintiff still insists that she only executed the charge document due to duress and coercion exerted on her, by the husband. In effect, the issue is one which I feel cannot be resolved on the basis of the conflicting affidavit evidence, so far available. The learned authors of “Chitty on Contracts” (28ed) Volume 1, stated, at 448 (paragraphs 7-070) that: “Where the creditor is aware that the debtor and surety are husband and wife, and the transaction is on its face not to the financial advantage of the surety as well as the debtor, the creditor will be fixed with constructive notice of undue influence, misrepresentation or other legal wrong by the debtor unless it has taken reasonable steps to satisfy itself that the surety has entered into the obligation freely and with knowledge of the true facts.” In the circumstances, I find that this is a ground upon which the plaintiffs have satisfied me that they have a *prima facie* case with a probability of success, because the suit property is registered in their joint names. In other words, if the trial court were to hold that the second plaintiff was the victim of duress or coercion, the validity of the charge instrument would be voided. I also find that if the suit property was to be sold off before the suit was heard and determined, the plaintiffs would suffer irreparable loss which may not be compensatable in damages. But, as I stated at the outset, that alone would not be a reason enough to warrant an injunction. However, the combination of the facts herein, including the possibility that the demand for the recovery of a debt which was in excess of the maximum recoverable pursuant to section 39(1) of the Central Bank of Kenya Act; the fact that there was probably some duress exerted on the second plaintiff; coupled with the fact that the facility secured by the suit property did not directly benefit the second plaintiff, causes me to find that the loss of the property in the circumstances would be incapable of compensation. Accordingly, there shall now issue an injunction to restrain the defendants, their agents, servants, advocates or any of them from advertising, disposing off, selling by public auction or by private treaty, leasing, or in any other manner howsoever interfering with the plaintiffs’ occupation and ownership of Land Reference number 3734/1168 (Land Reference number 78994) until this suit is heard and determined.

The costs of the application dated 10 January 2006 are awarded to the plaintiffs.

For the appellant:

*Infomation not available*

For the respondent:

*Information not available*