IN THE HIGH COURT OF TANZANIA

(MWANZA DISTRICT REGISTRY)

<u>AT MWANZA</u>

CIVIL APPEAL NO. 09 OF 2019

(Appeal from the judgement and decree of the Resident Magistrates' Court of Mwanza at Mwanza (Hon. Ngimilanga, RM) in RM. Civil Case No. 76 of 2015 Dated 31st October, 2018)

KIRUMI INSURANCE BROKERS LIMITED .... APPELLANT

VERSUS

EXIM BANK TANZANIA LIMITED .... RESPONDENT

<u>JUDGMENT</u>

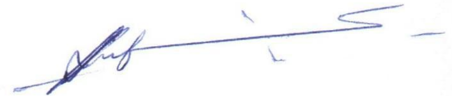
11th August, & 30th September, 2020

<u>ISMAIL, J</u>.

The matter that bred the instant appeal has had a varied past, that has seen it undergoing a trial, twice. In between the two trials, it was escalated to this Court by way of appeal which ultimately brought the parties back to the drawing board. It all began with a plaint which was instituted in the Court Resident Magistrates' Court of Mwanza at Mwanza, vide Civil Case No. 76 of 2016. In these trial proceedings the plaintiff's

(now the appellant) claim was, *inter alia,* for a refund of the sum of TZS. 12,812,406.71, that was held as an FDR in account No. 0062014649. This sum was allegedly withdrawn from the appellant's account to settle its indebtedness to the respondent. The appellant contends that by withdrawing the sum from the FDR account, to settle the alleged indebtedness, the respondent had reneged on its contractual undertaking of having the sum paid out upon maturity or realized as a collateral upon the appellant's in servicing the term loan. None of it applied in this case.

It all started on 30th April, 2013, when the appellant opened a fixed deposit account with the respondent (FDR Account No. 0062014649) into which the sum of TZS. 12,812,406.71, was deposited. On maturity, it was expected that the invested sum would increment to 17,053,314.71. Maturity of the FDR was expected on 30th April, 2015. In the subsistence of the FDR, i.e on 6th September, 2013, the appellant applied for a term loan facility of TZS. 10,000,000/- whose repayment period was 24 months from the date of issuance. The facility was to be secured by the sum in the FDR account. It is alleged that disbursement of the loan sum was delayed for 41 days until 17th October, 2013, when the said sum was credited into the appellant's account. During the 41 - day wait, the



appellant allegedly continued to issue cheques to settle its obligations with third parties and they were all honoured. On 15th October, 2013, the respondent allegedly unilaterally called on the sum in the FDR account, ostensibly to settle the sum overdrawn from the current account. Effectively, this meant that the sum was used to offset the loan sum which was advanced by the respondent through overdraws done through cheques.

This is what triggered the appellant's fury, hence the decision to institute the trial proceedings. The first round of the proceedings were concluded before Hon. Sumaye, SRM whose decision was not to the liking of either of the parties. They both appealed to this Court, vide Civil Appeal No. 58 of 2017. By the decision of the Court, delivered on 4th September, 2017, the matter was remitted back to the trial court for trial *de-novo*, owing to some glaring errors and omissions. It was further ordered that the re-trial should involve an expert in banking practice from whom his guidance would be enlisted. The matter in the re-trial was concluded in the respondent's favour by dismissing the appellant's claims. The trial court held the view that the respondent was justified in its decision to call on the sum in the FDR account to settle the sum which

was advanced to the appellant. The learned trial magistrate was convinced that the testimony of PW1, DW1 and exhibit D5 justified the respondent's actions. This decision did not go well with the appellant. It decided to take a ladder up to this Court on an appeal which has three grounds of appeal as follows:

1. *That the learned trial Magistrate erred, on the facts of the case, to hold that the Respondent was justified in utilizing the Plaintiff's money deposited in his FDR account with No. 0020146449.*
2. *That there is no evidence on record to support the learned trial Magistrate's holding that the Respondent advanced any loan to the Appellant.*
3. *The learned trial Magistrate erred in ignoring the Appellant's evidence and that of PW2, thereby arriving at the wrong decision.*

Hearing of the appeal was unanimously agreed to take the path of written submissions, preferred consistent with a schedule drawn and acceded to by the parties on 21st April, 2020. While the appellant enlisted the able services of Mr. Anthony Nasimire, learned advocate, the

respondent was ably represented by the ever present Ms. Marina Mashimba, learned counsel.

Hitting the first punch was Mr. Nasimire who chose to argue the grounds of appeal in a combined fashion. He took a swipe at the decision of the trial magistrate who held that the respondent was justified in its decision to utilize the appellant's sum in the FDR account to settle the latter's outstanding sum with the respondent. He contended that since the sum of TZS. 10,000,000/-, advanced through a loan agreement executed on 6th September, 2013 was repayable within 24 months of its disbursement, its servicing was to be done through Account No. 0060014837, and that the FDR account merely served as a collateral against the loan sum. With respect to disbursement of the loan sum, the learned counsel held the view that the sum was never disbursed as agreed and that, if it was, then the same was so disbursed after 40 days, and in contravention of the loan agreement which provided that the loan sum would be disbursed within 30 days of its execution. Mr. Nasimire further argued that at no point in time did the respondent inform the appellant that the loan sum would be disbursed after the expiry of the 30 days of execution of the agreement. Relying on clause 18 of the Offer Letter, Mr.

Nasimire contended that if the loan was not made available to the appellant within 30 days the contract would automatically expire, and his contention is that the same expired on 6th October, 2013. The learned counsel submitted further that if the said sum was disbursed on 17th October, 2013, as contended by the respondent, then that was an act of breach of contract since there is no evidence that the facility was validated after the expiry of 30 days contemplated under clause 19 of the Offer Letter. He contended, as well, that no evidence exists to show that the respondent informed the appellant of the validation of the sanction in terms of clause 18 of the Offer Letter.

Mr. Nasimire wondered as to why the sum in the FDR account was withdrawn and credited into account No. 0060014837, two days prior to the alleged disbursement of the loan sum. He contended further that there is no indication that the sum of TZS. 10,000,000/- was credited into account No. account No. 0060014837 before it was summarily debited from the said account, while the loan was for the term of 24 months, as provided for under clause 9, and the said period was yet to expire. The learned counsel decried the respondent's failure to serve any demand notice prior to its decision to effect a recovery. While maintaining that the

sum of TZS. 10,000,000/- was never disbursed to the appellant, the learned counsel implored the Court to order a refund of the sum of TZS. 12,812,406.71, which was debited from the FDR account. It is also prayed that this Court declares that the sum of TZS. 10,000,000/- was never paid to the appellant and, finally, that general damages be ordered for breach of contract.

In her rebuttal submission, Ms. Mashimba leapt to the defence of the trial court, contending that the decision sought to be impugned was based on a thorough evaluation of the available evidence, including the testimony of DW1. With respect to delays in the disbursement of the loan amount, the counsel's argument is that processing of the loan application was subject to adherence to some internal procedures and arrangements which are stipulated in Clause 15 of the Offer Letter (exhibit D2). These are the pre-disbursement arrangements whose satisfaction took the respondent up to 17th October, 2013, when the loan amount was finally disbursed. She contended that such delays were not a breach of the contractual terms as contended by the appellant.

Submitting on the appellant's contention that an FDR sum was debited from the FDR account to the loan account, the learned counsel

relied on exhibit D5, the bank statement, to dispel the contention that the sum of TZS. 10,000,000/- was debited from the FDR account. On the contrary, Ms. Mashimba argued, the sum of TZS. 12,103,135.99, that is alleged to have been withdrawn is the sum that had been overdrawn by the appellant at on 15th October, 2013. She further submitted that when the loan sum of TZS. 10,000,000/- was disbursed on 17th October, 2013, the same partly offset the overdrawn sum but it still left an outstanding balance of TZS. 2,203,135.99, due to the respondent.

Justifying the respondent's decision to recover the loan amount the very day the said loan was disbursed, the learned counsel for the respondent held the view that in view of the overdrawing of the account, the loan amount had to partly satisfy the overdrawn sum. With respect disbursement of the loan amount, Ms. Mashimba was emphatic that the appellant acknowledged that the loan amount was disbursed, and this concession is found in paragraph 13 of the plaint.

On whether a notice was served with a demand notice prior to the recovery of the loan amount, the respondent's counsel argued that the respondent was not bound to serve the notice of default as Clause 16 of exhibit D2, read together with paragraph 1 of the annexure 1 to D2 and

paragraph 7 of annexure 2 allowed recovery of the outstanding sum due without issuing a demand notice. The learned counsel contended that it is an undisputed fact, as testified by PW1, DW1, and as evidenced by exhibit D5, the loan sum had not been paid, an act which constituted a default, and it entitled the respondent to exercise its right under exhibits D2 and D3, and call for a sum in the FDR, allegedly kept as a lien to secure the loan advanced to the appellant.

Ms. Mashimba wound up by urging the Court to uphold the decision of the trial court and dismiss the appeal with costs.

In his rejoinder submission, the appellant's counsel still wondered why the sum of TZS. 10,000,000/- was used to settle the loan amount while the loan recovery period of 24 months had not expired. While denying that this arrangement was sanctioned by the appellant, Mr. Nasimire was also perplexed as to how would the cheques issued by the appellant be honoured while the respondent is contending that the account had been overdrawn. The learned counsel argued that if the account had no sufficient balance, then it was wrong to honour the cheques. To buttress his contention, he cited Halsbury's Law of England, 3rd edition, in which it is stated that a bank is not bound to let his customer overdraw his

account where there is no express or implied agreement in that respect. The learned counsel contended that, if it is true that that the account was overdrawn, the respondent had desired that the account be overdrawn. Alternatively, such acts exhibited negligence on the part of the respondent and, in the absence of any evidence that the appellant applied for an overdraft, using the FDR sum to net off the overdraft was an erroneous act. On this, Mr. Nasimire cited the case of ***The National Bank of Commerce v. Said Ally Yakut*** [1989] TLR 119.

Submitting on the respondent's contention that the FDR sum which was put as a lien to secure the loan, and that the sum was subsequently applied to settle the overdraft, Mr. Nasimire read mischief. He held the view that the respondent's contention is far from clear if not confusing about what exactly the FDR amount was spent on. He argued that he was at loss to comprehend if the FDR amount was used to offset the overdraft or it was channeled towards settling the loan amount. He contended that, since the FDR was a collateral that secured the loan and the respondent had not defaulted or reneged on its obligation to pay, then the respondent's action was erroneous. The learned counsel expressed his amazement as to how, if the FDR sum was spent on settling the overdrawn

amount, the respondent was not pressing to be paid the loan amount whose repayment is yet to be effected. He contended that this mix up is what shows that the respondent's action was unjustified. He urged the Court to allow the appeal.

From the parties' captivating submissions, the grand issue for this Court's settlement is mainly twofold: one, whether the appellant was advanced loan sum of TZS. 10,000,000/-; and two, whether the respondent was justified to utilize the sum in the FDR account to settle the appellant's outstanding obligation.

It suits me well to begin my disposal journey by first tackling the first question. Was the appellant advanced any loan? Is there any evidence to that effect? From the record of the proceedings in the trial court, there appears to be no dispute that, vide the appellant's letter dated 6th September, 2013, an application for a loan was lodged with the respondent. In the said letter, the appellant pledged its FDR No. 00662014649, then held by the respondent, as a collateral against the loan sum. This letter was attached to the appellant's statement of claim (plaint) as Annexure KRM 3. In response to the application, the respondent issued a Letter of Offer, dated 6th September, 2013 (exhibit D1), in which terms

and conditions for the issuance of the short term loan facility were set out. The facility had a repayment period of 24 months from the date of disbursement. Going by exhibit D4 (bank statement), the loan amount was disbursed to the appellant on 17th October, 2013.

The appellant is also on record acknowledging that the loan amount was credited into its account. This is gathered from the amended Plaint which was filed in the trial court on 21st November, 2017. In paragraph 13 of the amended Plaint the plaintiff is quoted as stating:

> *"That upon further enquiry it was learnt that the loan was disbursed on 17th October, 2013 being forty one (41) days from the date of signing the letter of offer.* ***A copy of the bank statement for the current account No. 0061004837 is annexed herein marked 'KRM-5' to which leave of this Court is craved that the same read as one with the plaint.****"*

Then in paragraph 15, the appellant stated as follows:

> *"That the defendant were in breach of the loan agreement when they disbursed the loan forty one (41) days after the signing of the letter of offer without notifying the plaintiff."*

From the evidence adduced during the trial and, going by the plaintiff's own admission as quoted above, I do not find anything to

support Mr. Nasimire's spirited contention that the loan amount was not disbursed to the appellant. I am overly convinced that the trial magistrate was quite in order when she answered this issue in the affirmative. This effectively settled the second ground of appeal by stating that there is sufficient evidence to support the contention that the appellant's application for short term loan was approved and disbursement of the loan was duly effected.

The next pertinent question relates to the respondent's decision to utilize the FDR sum to settle the appellant's indebtedness. Was this decision justified? While the appellant holds the view that this was uncalled for and premature, the view held by the respondent is that its decision was justified by the provisions of Clause 16 of the Letter of Offer and covenants set out in Annexures 1 and 2 to the Letter of Offer. I will spend a considerable time to review propriety or otherwise of the respondent's decision.

From the parties' submissions, and gathering from the pleadings, it is an undisputed fact that the loan was applied against an FDR account which served as a collateral against the said loan. What purpose does the collateral serve in loan applications?

"Collateral is an asset or property that an individual or entity offers to a lender as security for a loan. It is used as a way to obtain a loan, acting as a protection against potential loss for the lender should the borrower default in his payments. In such an event, the collateral becomes the property of the lender to compensate for the unreturned borrower." This can be in different forms, including cash. In the case of the latter, an individual can take a loan from the bank where he maintains active accounts, and in the event of a default, the bank can liquidate his accounts in order to recoup the borrowed money (See: *www.corporatefinanceinstitute.com*)

In the instant case, the appellant was allowed to overdraw its account through 15 (cheques) instruments (exhibit D4) the total value of which was TZS. 10,279,305/-. These withdrawals ranged between 6th September and 11th October, 2013. The first withdrawal through cheque was effected when the applicant's account had a balance of TZS. 134,117.32, while the last withdrawal was effected on 11th October, 2013, while the account had a paltry balance of TZS. 261,000/-. All of these credit balances were not sufficient to honour the appellant's obligations in the cheque. This means that the appellant was unilaterally allowed to overdraw the account. A legitimate overdrawing of an account can only be

done where a banker and its customer so agree through an overdraft agreement duly executed by the parties.

An overdraft, as defined in **INVESTOPEDIA**, quoted in the case of ***Exim Bank (Tanzania) Limited v. Dascar Limited & Another,*** CAT-Civil Appeal No. 92 of 2009 (unreported), means:

> *"An extension of credit from a lending institution where an account reaches zero. An overdraft allows the individual to continue withdrawing money, even if the account has no funds in it. Basically the bank allows people to borrow a set amount of money.*
>
> *"As with any loan, you pay interest on the outstanding balance of an overdraft."*

At p. 9:

> *"Logically, this means, that an overdraft facility is extended to a customer of a bank to overdraw his current account."*

In this case, there is no dispute that no overdraft agreement was executed by the parties. This means that any allowance for overdrawing the account by the appellant was wrong and the respondent's recourse was to dishonor the cheques. This would alert the appellant that its account has insufficient funds which would call for a funding arrangement.

If the appellant persisted with such indulgence the resultant consequence would be desirable and bordering on criminality. Subsequent overdrafts by the appellant were validated when the respondent allowed encashment of the first cheque and this built an erroneous but legitimate impression, by the appellant, that the account had sufficient funds to meet the appellant's obligations.

The contention made by the respondent is that there was an anticipation that the term loan would be disbursed. I don't find this to be a reason plausible enough to justify the respondent's "*kamikaze*" conduct. The appellant's account would only be capable of meeting the obligations in the cheques if and when the same had been credited with the loan sum. The anticipatory withdrawal effected by the respondent was not only un-businesslike but also against the banking norms.

The other pertinent question relates to how would the respondent use the term loan to offset the amount that was withdrawn in excess of TZS. 10,000,000/-, if the appellant was to be advanced the sum that does not exceed the TZS. 10,000,000/-? This has not been addressed by the respondent and it left the feeling that the stance taken by the respondent was not well thought about.

The respondent contends that the FDR amount was converted into the respondent's property when the appellant reneged on its financial obligations. This was allegedly consistent with the covenants stipulated in the Letter of Offer and the Credit Facility Agreement. For record, the FDR sum was converted on 18th November, 2014.

As stated earlier on, the FDR funds served as a collateral which was to secure the term loan against any default. It would be realized as and when an event of default occurred and upon issuance of notice of default, pursuant to Clause 16 of the Letter of Offer and such other covenants annexed thereto. The notice of default would require the appellant, the defaulter, to remedy the situation lest it placed itself in a precarious position. The nagging question is whether this was done. As unanimously submitted by both counsel, this was not done. As we ponder the consequence of not issuing the notice, the next crucial issue is whether there was any default.

The respondent's counsel has maintained that there were events of default whose occurrence was not communicated to the appellant. The view held by the respondent's counsel is that the appellant did not service the term loan and that such failure constituted an act of default which

justified the action that the respondent took. Its contention is based on exhibit D5, the bank statement.

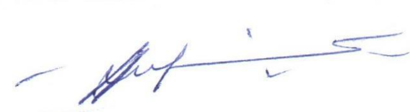
I find nothing propitiating in this contention. My contention is predicated on what is provided in Clause 16 of the Letter of Offer which states as follows:

Events of Default

"The Bank reserves its right to recall the entire liability/ies outstanding under the various facilities sanctioned to the Borrower as detailed above, together with accrued interest thereon, on the happening or occurrence of any of the "Events of Default", more fully described in Annexure 1 hereto, ***provided however the borrower(s)/guarantor would be given due opportunity to remedy the defect/set right the deficiencies within the time specified in the said Annexure.***" [Emphasis supplied]

This Clause takes me to Annexure 1, titled EVENTS OF DEFAULT, whose preambular provision states as follows:

"An "event of default" shall be deemed to occur upon the happening of any one or more of the events specified hereunder. The Bank reserves its right to recall the entire liability/ies outstanding under the various credit facilities sanctioned to the Borrower, together with accrued interest



*thereon, on the happening or occurrence of any such "Events of Default". **Before resorting to such action, the Bank, though not bound to do so, will serve the notice to the to the Borrower(s)/guarantor(s) to initiate remedial measures to set right the defect/deficiencies within 15 days from receipt of such notice. If the Borrower(s)/Guarantor(s) fail to set right/rectify the same to the satisfaction of the Bank within the period specified herein or such extended period as the Bank may permit at its sole discretion, the Bank shall proceed ahead with initiation of the recall of the advance.'*** [Emphasis is mine]

In both of these Clauses, the emphasis is that events of default must be communicated to the borrower, the appellant herein, through a notice, and that such notice should require the defaulting borrower to right such wrongs, and the time frame provided is 15 days.

A further illustration of the importance of the default notice was accentuated in ***LaSalle Bank v. Kelly***, C.A. No. 09CA0067-M. In the cited case, the Court of Appeals for the Ninth Judicial District of Ohio reversed the trial court's judgment for foreclosure, due to the mortgage holder's attorney's failure to allege in the complaint, even generally, that the

mortgage holder had delivered the required notice prior to acceleration of the debt. Even though the borrowers did not raise the defence in their answer to the complaint, the Court decided that the borrowers were nevertheless entitled to raise that defence, for the first time, in their brief in opposition to the plaintiff's motion for summary judgment."

To give a wide scope to what has been stated above, Preeti Kulkarni, a Banking and Management Consultant, wrote of the rights of loan defaulters. In the article published in ***The Economic Times*** on 11th April, 2016, he stated as follows:

> *"A default does not strip of your rights or make you a criminal. Banks have to follow process and give you time to repay dues before repossessing your assets to realise the arrears. If the borrower's account is classified as non-performing asset, where repayment is overdue by 90 days, the lender has to first issue a 60-day notice to the defaulter.... If the borrower fails to repay within the notice period, the bank can go ahead with sale of assets. However, in order to sell, the bank has to serve another 30-day public notice mentioning details of the sale."*

Noteworthy, the views expressed above are in sync with the Court's holding in the ***Registered Trustees of Africa Inland Church Tanzania***

v. CRDB Bank PLC & 2 Others, HC-Comm. Case No. 7 of 2017 (unreported), in which it was held that failure to serve a notice of default or failure to see out the notice period is fatal and has the impact of rendering the foreclosure illegal and ineffectual.

In view of the foregoing position, as gathered from the cited authorities, I hold an unflustered view that, since there is no evidence of default of the terms of the loan agreement and, in the absence of the notice of default issued by the respondent, realization of the collateral was premature and was not actuated by any default. It was, therefore, an act of wanton disregard of the procedural requirements set out in the Letter of Offer. It constituted an affront of the banking norms and best practices. Furthermore, this hastened call on bordered on a breach of the loan agreement, as the respondent realized what was set out to be realized in 24 months or on the appellant's failure to honour its obligations. It is my considered view that it was erroneous and utterly unjustified for the respondent to realize the FDR sum which secured a loan whose servicing had not been defaulted. I find the second ground of appeal meritorious and I allow it.

In the third ground of appeal, the appellant decries failure of the trial magistrate to consider the testimony of PW2 in her decision. This ground of appeal was not covered by the counsel's submission. My scrupulous review of the proceedings confirms that PW2 testified in support of the appellant's case. His testimony dwelt on what he thought were the procedures as they obtain in other banks. While PW2's testimony did not have a direct bearing on what the respondent allegedly erred in handling the appellant's loan application, it was inappropriate for the trial court to give such evidence a wide berth. The learned magistrate ought to have made an assessment of what the witness testified and make a finding thereon. As I agree with the appellant that this was a flawed indulgence by the trial magistrate, I wish to hasten that such failure did not occasion any injustice, considering the fact that this testimony was not of any direct probative value. It contains the "oughts" as they obtain in other financial institutions. These "oughts" bore no significance to this matter. It is my firm contention that this anomaly would not have the effect of altering the equation.

In the upshot of all this, I find merit in the appeal and allow it. I, as a result, order as follows:

(i) That the FDR amount which was irregularly converted should be refunded back, plus interest to the date of maturity;

(ii) Interest on (i) from the date of maturity of the FDR to the date hereof at the rate set for investment in the FDR, less any outstanding sum due to the respondent, arising out of the unsettled balances on the term loan;

(iii) Costs of this appeal.

It is so ordered.

Right of appeal duly explained to the parties.

DATED **at MWANZA** this 30th day of September, 2020.

M.K. ISMAIL

JUDGE