

DRAWING THE LINE ON EXPLOITATIVE LENDING:
THE CASE OF A KES 4M LOAN SPIRALING TO KES 69B

"Courts do not rewrite contracts for individuals who belatedly realize they entered into bad bargains. However, courts do not enforce unconscionable contracts either."

What happens when a loan interest exceeds 1,724,900%? With tough economic times, some lending institutions have taken advantage of borrowers by advancing loans at exorbitant interest rates. In some cases, the rates have been so extreme that they have "shocked the conscience of the Courts!"

In a bold and nuanced decision, the Court of Appeal has reaffirmed that the scales of justice in Kenya will not tilt in favour of oppressive contracts, no matter how sophisticated their terms. In **Kanwal Sarjit Singh Dhiman v Keshavji Jivraj Shah [2025] KECA 1264**, the Court delivered a defining pronouncement on the intersection of contract freedom, informal lending, unconscionability, and the enduring reach of equity. Let us take a deeper look into the case and examine what makes it a locus classicus in lending.

BACKGROUND

The dispute originated in **1996**, when the respondent agreed to lend the appellant **KES 13 million**, to be advanced in tranches. Only **KES 7 million** was disbursed, as the appellant defaulted before the final amount could be released. The loan attracted a striking **36% per annum interest, compounded quarterly**.

The respondent moved swiftly, obtaining an **ex parte judgment** in **1999**, leading to the public auction and vesting of the appellant's prime property. But in **2015**, that judgment was set aside by the Court of Appeal and the case sent back for retrial. Despite this, the High Court in **2019** upheld the respondent's title and declared the agreement valid.

It is against this backdrop that the matter returned to the Court of Appeal. The issues raised touched the core of how Kenyan courts treat post-judgment transactions, private lending without a license, and the limits of fairness in finance.

ISSUES FOR DETERMINATION

The Court distilled the appeal into four central questions:

1. Do execution orders—like vesting of property—survive once the judgment they are based on is set aside?

2. Can a loan agreement between private parties be enforced if it contains oppressive and disproportionate terms?
3. Was the respondent's suit filed prematurely under the loan agreement?
4. Was the appellant's counterclaim time-barred?

Each question invited the Court to weigh strict legality against equitable intervention.

JUDGEMENT: WHEN LAW YIELDS TO EQUITY

1. Consequential Orders Cannot Survive a Vacated Judgment

The respondent's title was founded on an ex parte judgment. Once that judgment was set aside, the Court held, all resulting orders—including the vesting order and the auction sale—were automatically void.

> *"To maintain the vesting order would be to defeat the very essence of the retrial directed by this Court in 2015,"* the Court observed.

Result: The respondent's title was cancelled, and the property was ordered to revert to the appellant.

2. Unconscionability Renders Contracts Unenforceable

While the Court accepted that **private lending is not illegal**, it drew a firm line at **oppressive terms**.

The loan agreement provided for a 36% annual interest rate, compounded quarterly terms that would exponentially inflate the KES 4 million unpaid balance into a sum exceeding **KES 69 billion**.

> *"A court of equity cannot enforce a contract whose effects are unconscionable, regardless of the sophistication of the borrower or the legality of the document,"* the Court held.

While the doctrine of **freedom of contract** remains a bedrock principle, the Court emphasized that it is **not absolute**. The law will not enforce bargains that "shock the conscience" of the court.

Result: The agreement was declared void and unenforceable.

3. Breach by the Borrower Justified the Suit

The appellant argued that the suit was filed prematurely since the loan term had not matured and a charge over the property had not been created.

The Court disagreed, finding that the appellant's default in repaying the initial tranches **frustrated the agreement**. The lender had no obligation to disburse the balance once the borrower was in breach.

Result: The claim was properly filed and maintainable.

4. The Counterclaim Was Based on Property, Not Time-Barred

The High Court dismissed the appellant's counterclaim as time-barred, holding that it was filed after the six-year limitation period. However, the Court of Appeal took a different view, finding that the counterclaim was founded on proprietary rights rather than breach of contract, and was therefore subject to the twelve-year limitation period applicable to land claims. However, having already ordered the restoration of the title to the appellant, this issue was rendered academic.

5. Equitable Restitution: The Borrower Must Repay What Was Received

Though the loan agreement was void, the Court held that the borrower could not retain the **KES 4 million** he had received without consequence.

Invoking the equitable doctrine of **unjust enrichment**, the Court ordered restitution with interest at **12% per annum**, the statutory court rate, from 19th September 2019.

"Equity will not permit a man to profit from his own default. The appellant must repay what he received—no more, no less."

If unpaid within 90 days, the respondent would be entitled to **recover the amount through lawful sale** of the property—an orderly and equitable path.

6. The Broader Implications: Fairness, In Duplum, and the Role of Courts

Although the Court did not directly invoke the in duplum rule under Section 44A of the Banking Act, its reasoning paralleled the principle's core purpose: to prevent a debtor from being crushed by runaway interest accumulation.

While this rule applies strictly to banks and financial institutions, the Court's decision in Dhiman signals that equity serves as a broader, more flexible safeguard, especially in private lending.

CONCLUSION

The **Dhiman** decision is a watershed moment in Kenyan commercial jurisprudence. It affirms that:

- Courts will invalidate contracts that offend basic fairness, no matter how artfully drafted.
- Execution orders fall with the judgment that birthed them.
- Private lending is permissible, but its terms must survive equitable scrutiny.
- Unjust enrichment will not be permitted under the guise of a void contract.

At its core, this judgment reinforces a vital truth: contracts are not immune to conscience. Where a deal crosses the threshold into oppression, the law will not lend its authority to **enforce it**.

For lenders, borrowers, and commercial advisors, the message is clear—**document your transactions well, price them responsibly, and anticipate judicial intervention where fairness is absent**.

HOW WE CAN HELP

At **CM Advocates LLP**, we remain at the forefront of protecting commercial integrity and advising clients on legally enforceable and commercially sound lending structures. Whether you are a private lender, borrower, or investor, our commercial litigation and banking law teams are ready to assist you in navigating this evolving legal landscape. Reach out to us via ***law@cmadvocates.com*** or contact our contributors.

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