

INSOLVENCY OF A DEVELOPER AND/OR PROPERTY OWNER CAN A CLAIM FOR UNJUST ENRICHMENT BE SUSTAINED AGAINST A LENDER BY THE CONTRACTOR?

INTRODUCTION:

In instances where a property owner and/or developer is faced with insolvency proceedings, the developer risks being left with no way of recovering funds expended in the construction project especially in instances where there is an existing charge registered in favor of a bank (Chargee) over the property in question. In this article, we explore the circumstances under which a claim for unjust enrichment can be sustained against the lender in such cases as a remedy for a contractor in respect of unpaid dues by the developer and/or property owner.



Contractors' Lien: In ordinary circumstances, where there is no charge registered over a property, contractors have a common law remedy against the owners known as a contractor's lien. This lien allows the contractor to retain possession of the property until the debt owed by the owner is paid in full.

However, when there is a charge registered over a property, the contractor's lien being an unregistered interest cannot supersede the Bank's registered interest and this has been affirmed by variously. More specifically, where the owner and/or developer defaults on loan repayment, the Chargee has the right to exercise its statutory power of sale and the same cannot be limited by a contractor's lien unless there are special circumstances as further discussed herein.

Case in point: China Wu-Yi Company Limited vs. Suraya Property Group Limited and 2 Others ML HCC No. 76 of 2019 [2020] eKLR

Summary of facts: The Plaintiff, a construction company, filed an application seeking injunctions to restrain the Defendants from dealing with houses pending the hearing and determination of the suit. The 2nd Defendant, the property owner had charged the property to the 3rd Defendant to finance the project. The Plaintiff's claim was based on the fact that when it was apparent that the 2nd Defendant was not able to pay it for the construction work, it got into an agreement for payment in kind by purchasing some of the developed units. In this regard, it argued that it held a purchaser's lien over the houses and therefore should continue to be in occupation until fully paid. Additionally, it argued that as the contractor who improved the property by investing its resources, it also had a builder's lien over the property.

Bank's Argument: The Bank argued that it had not given consent for the houses to be sold and, as there was a charge registered in its favor, its rights could not be defeated.

Court's Finding: The court found that the purchaser's lien based on the sale agreement and the builder's lien based on the construction services rendered to the 1st Defendant were enforceable only against the 1st Defendant and not the Bank. In the circumstances, the court found that the Plaintiff lacked any registered or other interest that would defeat the Bank's charges.

In this regard, the remedy available to the contractor in instances where the bank holds a charge over the developed property, is against the borrower, as the contract exists between the contractor and the borrower, not the Bank unless the Bank represents to the contractor that it shall not exercise its statutory power of sale on account of the contractor's debt.

More specifically, if the Bank requests the contractor to proceed with the construction of the property and gives an undertaking to settle all dues owed to the contractor, the contractor may institute a claim of unjust enrichment against the Bank. Unjust enrichment occurs when one party confers a benefit upon another at its own expense. To sustain a claim for unjust enrichment, it must be proven that a party has been enriched at the expense of another party, and there is no reason justifiable in law to allow the enrichment.

UNDER WHAT CIRCUMSTANCES CAN A CLAIM FOR UNJUST ENRICHMENT BE SUSTAINED AGAINST A LENDER BY THE CONTRACTOR?

Unjust enrichment is one of the causes of action available to contractors against a lender and/or bank in instances where a developer and/or property owner is subjected to insolvency proceedings exposing the contractor to the risk of inability to recover funds owed under the construction contract.

Elements of unjust enrichment: To sustain a claim for unjust enrichment, three elements must be present:

a. The party has been enriched by receiving a benefit.

b. The party has been enriched at the expense of another party.

c. There is no legal reason to allow the enrichment.

Case in point: Chase International Investment Corporation and Another v Laxman Keshra and 3 others [1978] Eklr

Summary of facts: Chase International Investment Corporation (Chase), an investment corporation, entered into an investment loan agreement with a property owner to facilitate the development of the property. Laxmanbhai (the Plaintiff), a firm of contractors, had been retained by the property owner to construct lodges on the property. However, the property owner became insolvent and could no longer repay the loan. Chase despite being aware of the insolvency assured the contractor that they would pay them once the construction was completed. Based on this assurance, the contractor continued with the construction work and completed it on time. A receiver was appointed over the insolvent company, the property sold and the proceeds were paid to Chase. The contractor, as an unsecured creditor, sued Chase in the High Court, claiming their dues of Kshs. 1,843,007/- on the basis of alleged express contract, fraudulent misrepresentation, and the principle of unjust enrichment.

Trial Court's Decision: The High Court held that the contractor failed to prove the alleged contract and fraudulent misrepresentation. However, the court found that Chase, by enforcing its security under the debenture trust deed and taking advantage of its legal rights, acted unconscionably, inequitably, and unjustly.

Court of Appeal's Decision: The Court of Appeal, in dismissing the appeal by Chase, upheld the principle of unjust enrichment. The court held that; Chase was enriched by receiving a benefit (Laxmanbhai's labor and services), it was enriched at Laxmanbhai's expense, and it would be unjust to allow Chase to retain the benefit fully. It stated that mature legal systems provide for the restoration of ben-

efits on grounds of unjust enrichment in various circumstances. The court emphasized that the appellants (Chase) had been enriched at Laxmanbhai's expense and that it would be unjust to allow them to retain the benefit to the full extent of Laxmanbhai's claim.

CONCLUSION

In cases where a bank (lender) requests a contractor to proceed with construction and gives an undertaking to settle all dues, but later

wishes to carry out its power of sale before the contractor has received full payment, the contractor may have a remedy in a claim for unjust enrichment against the bank. This claim can be sustained if the three elements of unjust enrichment are present. Further, courts have held that such assurances and/or promises by the lender can be considered as guarantees creating enforceable contractual obligations. Case in point: **National Bank of Kenya Ltd v Devji Bhmji Sanghani & another [1996] eKLR**

HOW CAN WE HELP?

The Debt Recovery Restructuring and Insolvency team at CM Advocates LLP prides itself in having a wide variety of resources, skills, and experience on matters of Insolvency and debt recovery. We are practical and innovative in our approach and offer quick turnaround timelines. We will be delighted to receive your feedback and inquiries and offer our services in this and any other of our practice areas.

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