



Strathmore University
Law School

***IN DUPLUM* RULE IN KENYA: A CRITICAL ANALYSIS OF THE
UNADDRESSED ASPECTS OF SECTION 44A OF THE BANKING ACT**

**A DISSERTATION SUBMITTED IN PARTIAL FULFILLMENT OF THE
BACHELOR OF LAWS DEGREE**

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and guiding me along the way.

DECLARATION

I hereby certify that this dissertation constitutes my own product, that where the language of others is set forth, quotation marks so indicate, and that appropriate credit is given where I have used the language, ideas, expressions or writings of another.

I declare that the dissertation describes original work that has not previously been presented for the award of any other degree of any institution.

A handwritten signature in blue ink, consisting of a stylized, cursive 'C' followed by a series of loops and a horizontal stroke.

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Christopher Kiragu Ndegwa

incurred in the recovery of any amounts owed by the debtor may be recovered. This statutory rule has its rule in South African common law.

Kenyan jurisprudence has demonstrated a divergence from interpretations of the rule as per other jurisdictions where the rule has a long standing history such as South Africa. This is indicative of a misnomer which upon further interrogation reveals that section 44A of the Banking Act is merely a semblance of the in duplum rule and not the in duplum rule stricto sensu.

The aim of this paper is to scrutinise the rule while carrying out a comparative analysis in a bid to address the issue of whether our enactment of the in duplum rule will effectively serve the purpose for which it was enacted; protection of consumers of credit.

Ethekwini Municipality v Verulam Medicentre (PTY) Ltd [2005] ZASCA 98 (457/04).

Housing Finance Co. of Kenya Limited v Gilbert Kibe Njuguna Nairobi HCCC No. 1601 of 1999.

Husamuddin Gulamhussein Pothiwalla Administrator, Trustee and Executor of the estate of Gulamhussein Ebrahim Pothiwalla v Kidogo Basi Housing Corporative Society Limited & 31 others Civil Appeal No. 330 of 2003.

LTA Construction Bpk v Administrateur van Transvaal (112/90) [1991] ZASCA 147.

Mohammed Gulambussein Farzal Karnali & Another v CFC Bank Limited & Garam Investments HCCC No. 3 of 2006.

Paulsen and Another v Slip Knot Investments 777 (Pty) Ltd [2015] ZACC 5.

Pelican Investment Ltd v National Bank of Kenya Ltd [2000]2 EA 488.

Sanlam Life Insurance Ltd v South African Breweries Ltd 2000 (2) SA 647 (W).

Standard Bank of SA Ltd v Oneanate Investments (Pty) Ltd 1995 (4) SA 510 (C).

Stroebel v Stroebel 1973 2 SA 137 (T).

The *in duplum* rule is a rule of law which provides that when interest on a debt equates to the capital of the debt, interest ceases to continue accruing.¹ It seeks to protect the debtor from overexploitation by credit rendering institutions.

Having the objective of protecting borrowers from finding themselves entangled in a thread of debt that they cannot untangle; it has been generally described as being protective.² So great is this principle that it draws its roots from the Code of Hammurabi in 1800 B.C. that forbade a collection of interest greater than that which was lawfully due.³

This rule made its way into the legal framework of the financial service sector via section 44A of the Banking Act⁴ which stipulates the maximum that an institution can recover from a debtor with respect to a non-performing loan.⁵ Although this law seeks to provide protection of debtors from creditors, it has some ambiguities that if not addressed, may hinder the objective of the law.

There is a stark difference between the common law *in duplum* rule and the statutory *in duplum* rule. This divergence of concepts may lead to different applications of the rule and consequently, conflicting application of the law.

Further, a prima facie comparison of the *in duplum* rule applied in Kenya vis-à-vis that implemented in South Africa reveals a variance in interpretation of the rule meant to ease the chokehold that financial institutions would have on debtors. Perhaps this is because the rule in s 44A the Banking Act is merely a semblance of the *in duplum* rule. The ramifications of

1.2. STATEMENT OF PROBLEM

S 44A of the Banking Act does not sufficiently protect the consumer of credit and it is detrimental to credit providers as well credit consumers.

1.3. JUSTIFICATION OF THE STUDY

Addressing the obscurity surrounding this rule will render clarity on a number of potential issues that may arise. This can only be done after interrogating the mischief that the rule was meant to address and evaluating whether or not it is capable of serving its purpose or whether it is a structure with a faulty foundation. This evaluation ought to be carried out in the context of protection of the consumer of credit as well as safeguarding creditors.

This study seeks to spark a law reform that would see the *in duplum* rule clearly defined and equitably applied in the Kenyan atmosphere.

1.4. HYPOTHESIS

Section 44A merely enacted a semblance of the *in duplum* rule and as such, will not be able to serve the intended purpose for which it was enacted.

1.6. STATEMENT OF OBJECTIVES

1. Assessing the application of the rule to contracts that do not involve financial institutions.
2. Analysing what constitutes the interest that can be claimed by the creditor.
3. Assessing whether or not the rule stifles financial institutions under the pretext of consumer protection.

1.7. CHAPTER BREAKDOWN

Chapter 1: Introduction

Chapter 2: Historical background of interest rate laws in Kenya

Chapter 3: Comparative analysis between Kenya and South Africa on the application of the *in duplum* rule

Chapter 4: Restriction of the application of the *in duplum* rule

Chapter 5: Conclusion and recommendations

“If a man begets a son...who lends at interest and exacts usury – *this son certainly shall not live...he shall surely die; his death shall be his own fault.*”⁶

Throughout history, the regulation of interest charged on loans has always been a bone of contention. This has been so, to prevent usury – the practice of lending money to people at unfairly high rates of interest.⁷

The Code of Hammurabi dated 1750 B.C. regulated the interest that could be charged on a loan.⁸ The significance of this provision was to ensure that the borrower would not be extorted and hence, have his agricultural produce suffer.⁹ The Greeks shared similar sentiments regarding the regulation of interest. Both Plato and Aristotle believed usury was immoral and unjust. During the period of 800 – 600 B.C. the Greeks at first regulated interest, and then deregulated it. The consequences of deregulation were, *inter alia*, the creation of a colossal amount of unregulated debt as most Athenians had feeble pockets thus relied on loans from the wealthy that were accompanied by a hefty interest rate. The poor would then offer themselves as surety for the loan and upon default Athenians were sold into slavery.¹⁰

In the year 533 A.D. the Roman “Code of Justinian” set a graduated maximum interest rate that did not go over 8.3 % for loans to ordinary citizens.¹¹ Medieval Roman law treated

⁶ Ezekiel 18: 13 The African Bible Paulines Publications Africa 1999

the Council of Nicaea, passed a canon prohibiting usury by clerics and citing the Psalm 15.¹³ Pope Leo the Great forbade clerics to take usury and declared laymen who take it to be guilty of “shameful gain.”¹⁴ It is important to understand that this stance had its root in the traditional Christian view that earning interest was a wrongful action equitable to a sin. “...lend freely, hoping nothing nearby.”¹⁵

The Islamic faith shares this stance as it prohibits lending money at an interest (*riba*).¹⁶

Such was a position that was adopted by Charlemagne in 800 A.D. as he outlawed interest throughout his empire.¹⁷ It can be seen that such an approach would have stemmed from the conception that interest charged on credit would easily be prone to abuse by credit providers. This perception must have been an informed one as usurers were depicted in the lowest ledge in the seventh circle of hell – even lower than murders – by Dante in *The Inferno* which he penned over a fifteen year period beginning in 1306.

In the 18th century, the Church adopted a more tolerable approach towards interest-based lending.¹⁸ Concurrently, the wave of capitalism promoted the lending of money at a ‘cost’ as

¹² The History of Usury, Americans for fairness in lending, available at <
<https://americansforfairnessinlending.wordpress.com/the-history-of-usury/>> (accessed on 31/10/2015)

absence of a natural limit to the range of an individual's efforts in terms of profits – including interest.²⁰ This effectively means that persons ought to be permitted to recover any amount from their efforts so long as it is agreed upon by the parties.²¹

This is in contravention of the labour theory which postulates that one is entitled to the 'work of their hands'.²² The absence of a limit on the amount of interest that can be recovered from an advancement of credit can easily lead to the extortion of weaker parties as seen in preceding paragraphs. Exorbitant interest may be charged or inequitable payment terms may be enforced by the credit provider to trap the credit consumer in a maze of unmanageable debt.²³

In this regard, an efficient law ought to protect the consumer's economic interests²⁴ yet at the same time, ought to be equitable to all parties

2.2. ATTEMPTS TO REGULATE INTEREST IN KENYA: DONDE ACT

The Central Bank of Kenya (Amendment) Act 2001 – commonly referred to as the Donde Act – was a private member's bill introduced in Parliament in 2001 to control bank interest rates. The Bill sought to peg bank interest rates to Treasury Bill rates as well as establish a monetary policy committee. This was an attempt to place reins on an already out of control banking system that had suffered the effects of deregulated interest rates due to the Banking Act of 1993.²⁵ Such deregulation was ignorant of the oligopolistic nature of the Kenyan banking system and had led to collusion between certain banks whose increased interest rates

thereby safeguarding the exorbitant profits that banks would make from lending at such extortionist interest rates. This would translate into handsome returns that they received on their investments – the donor funds that had been invested in the banks.²⁸ Many Kenyans supported the bill in its quest to curb the usurious habit of banks and scale down the suffering of Kenyan consumers of credit.²⁹

Although the Kenya Bankers Association (KBA) acknowledged the unfriendly interest rates, it opposed the Bill due to its retrospective application. The Act came into force on 6 August 2001 but its commencement date was 1 January 2001. KBA challenged the constitutionality of this provision as section 77 of the then Constitution protected persons from retrospective application of criminal sanctions as it contravened their right to a fair trial. The High Court held that the provision on the retrospective application of criminal sanctions was unconstitutional.³⁰ Those provisions touching on the non-criminal civil aspects of the Donde Act were still in force. One of such integral provisions was that the maximum interest rate chargeable on all loans and advances from 1 January 2001 was “*the 91-day Treasury-Bill rate published by the Central Bank of Kenya on the last Friday of each month, or the latest published 91-day Treasury Bill rate, plus 4 per centum*”.³¹

This position was buttressed by the Ochieng J in *Mohammed Gulambussein Farzal Karnali & Another v CFC Bank Limited & Garam Investments*³² where he stated that the Act had come into force on 1 January 2001 thereby connoting the validity of the Act notwithstanding those elements that had been declared to be unconstitutional.

principal sum is a precursor to the *in duplum* rule.

One of the arguments advanced by the antagonists of the Donde Bill was that the manner measures the Bill sought to implement to regulate interest rates would have adverse economic effects. The IMF made an ‘offer’ to send experts to the Office of the Attorney General and to Central Bank; an offer whose refusal would be reciprocated with a withholding of aid.³⁴ At the same time, efforts to have government regulate oil prices led to an outcry against the same by the United States with the then Ambassador to Kenya, Johnnie Carson, advising Kenyan MPs that, “*Credit, like petrol, is a commodity*” that would dry up if wrong laws and policies such as those being proposed were implemented.³⁵ Many classified this as modern colonialism.³⁶

Unfortunately, this Act was repealed and can be classified as a piece of still born legislation; its true intended effects were never felt.

2.3. INTRODUCTION OF THE *IN DUPLUM* RULE

The *In duplum*³⁷ rule generally provides that unpaid interest ought to stop running once it equals the unpaid capital amount.³⁸ This, in principle, ought to prevent the consumer of credit from paying interest that is greater than the capital sum advanced to him/her.³⁹ This was introduced into the Kenyan legal framework regulating the banking sector via section 17 of the Banking (Amendment) Act that resulted in the inclusion of section 44A in the Banking Act, CAP 488 Laws of Kenya.

This not only clearly establishes when interest on a non-performing loan ought to stop running, but it also outlines the elements that comprise the recoverable sum from the debtor. This has, to some extent, carried out the intention of the Donde Act of ensuring that borrowers are not extorted into paying back more than double the principal amount accorded to them by credit-rendering institutions.

The 1972 reiteration of the rule by the South African Transvaal Provincial Division has often been quoted as being one of the most succinct that stated, “...for the statement that interest may not exceed the amount of the capital itself, as soon as the interest reaches an amount equal to the capital the interest ceases to run, if the accrued interest or a part thereof is paid, it starts to run again, but again only until it is again as high as the capital.”⁴¹

Interestingly enough, the terminology ‘*in duplum*’ has been regarded as being technically incorrect as the rule itself prohibits charging of more than twice the capital. In *Commercial Bank of Zimbabwe v MM Builders (Pty) Ltd*⁴², Gillespie J states that the proper reference to this rule ought to be ‘*ultra duplum*’. This is because although the rule prohibits more than double the capital, it *allows* less than double; and only prohibits beyond double the capital amount when the interest is in arrears.⁴³

There have been, however, numerous questions raised on whether the *in duplum* rule is fit for its intended purpose. It has been posited that its application in the Kenyan context may yield different results from those which it was intended to yield. The simultaneous application of

indeed the codification of the *in duplum* rule *stricto sensu* or whether it is a mere semblance of the same.

3.1. COMMON LAW V STATUTORY *IN DUPLUM* RULE

3.1.1. COMMON LAW *IN DUPLUM* RULE

It is of utmost importance to note the existence of both the common law *in duplum* rule as well as the statutory *in duplum* rule. The former, as construed in South African law⁴⁶ and fortified through judicial precedence, provides that interest stops running when unpaid interest equals the outstanding capital amount. If the total amount of unpaid interest – both contractual and default interest, has accrued to an amount equal to the outstanding capital sum, the defaulting debtor must first start making payments on his loan again (and so decrease the interest amount), after which interest may once again accrue to an amount equal to the outstanding capital sum.⁴⁷

The rule thus effectively prevents unpaid interest from accruing further once it reaches the unpaid capital sum. Even if interest is capitalised and interest is therefore charged on interest, the capitalised interest does not lose its character as interest and become part of the capital amount for purposes of applying the *in duplum* rule.⁴⁸

Therefore, the common-law *in duplum* rule implies that the total amount of unpaid interest on a loan or credit transaction may accrue only to an amount equal to the outstanding capital sum and that all arrear interest ceases to run when that interest has reached the outstanding capital amount.⁴⁹ This rule was fortified in the case of *Sanlam Life Insurance Ltd v South*

as ne/she at no time allows the unpaid interest to reach the unpaid capital amount.⁵¹ Nevertheless, if this escalation occurs, interest ought to immediately cease to accrue. Once payments on the account are again made and the interest element of the total amount owed is decreased, the interest can start running again until it equals the outstanding capital. It is thus clear that the rule only prevents the interest from running on a temporary basis and does not set a maximum amount of interest that may be charged.⁵²

The common-law *in duplum* rule is not limited to interest on money-lending transactions. In fact, it applies with equal force to all types of contract in terms of which a capital sum is due by the debtor to the creditor and on which amount a specific rate of interest is payable. One such an example is where a debtor owes money to a creditor in terms of a contract of letting and hiring of work on which interest is payable.⁵³

3.1.2. STATUTORY *IN DUPLUM* RULE

The common-law *in duplum* rule has been codified into statute which is commonly referred to as the statutory *in duplum* rule.⁵⁴ One such example is that found in section 103 (5) of the National Credit Act of South Africa which states: *Despite any provision of the common law or a credit agreement to the contrary, the amounts contemplated in section 101(1) (b) to (g) that accrue during the time that a consumer is in default under the credit agreement may not, in aggregate, exceed the unpaid balance of the principal debt under that credit agreement as at the time that the defaults occurs.*⁵⁵

The statutory *in duplum* rule has been argued by some to provide greater protection to the

Since Kenya's history does not point towards any application of the *in duplum* rule prior to the amendment made to the Banking Act, it will be taken that all references to the *in duplum* rule in a Kenyan context refer to the statutory *in duplum* rule.

3.1.3. APPLICATION OF CLAYTON RULE TO *IN DUPLUM* RULE

The rule in Clayton's case⁵⁷ is that payments towards a running account, such as a bank account, are applied to the earliest debt first. Thus, the most recently incurred charge is the last charge that will be paid off.⁵⁸ This is commonly referred to as "first-in-first-out principle". The pertinent issue regarding the rule in Clayton's case is its concurrent application with the *in duplum* rule.

In *Standard Bank of SA Ltd v Oneanate Investments (Pty) Ltd*⁵⁹ Selikowitz J stated that when interest on the unpaid capital has reached an amount equal to it, then the effect of applying the *in duplum* rule would be to grant the debtor a double benefit that was not intended. This can be better grasped with the aid of an illustration.

The example of the cessation of KES⁶⁰1 000 arrear interest having accrued from an unpaid capital amount of KES 1 000 is apposite. If the debtor pays to the creditor KES 100, and the Clayton rule were to be applied, then KES 100 would reduce the capital amount. At the same time the *in duplum* rule would take effect with the implicative consequence of the

⁵⁶ See generally Section 103 (5) National Credit Act (South Africa) and Section 44A (2) Banking Act (CAP 488 Laws of Kenya).

⁵⁷ *Devaynes v Noble* (1816) 1 Merivale 529

instructs.⁶¹

It seems reasonable from the aforementioned example that any payments made ought to be appropriated to the interest first only before being appropriated to the capital.

3.1.4. CAPITALISATION OF INTEREST

The capitalisation of interest is an aspect of loan repayments from which confusion has arisen in the past regarding the application of the *in duplum* rule.⁶² This is because the capitalisation of interest has been argued to change the nature of interest thereby leading to many considering it as capital and not interest for the purposes of application of the *in duplum* rule.⁶³ This was seen in the case of *Standard Bank of SA Ltd v Oneanate Investments (Pty) Ltd*⁶⁴ where Standard Bank argued that interest, once capitalised, changes its nature and is then considered as capital.

One of the main arguments of Standard Bank was that the *in duplum* rule ought not to apply to overdraft accounts as interest was almost immediately capitalised in such accounts. Selikowitz J in his judgement stated that “...words like 'capitalisation' are used to describe the method of accounting used in banking practice. However, neither the description nor the practice itself affects the nature of the debit. Interest remains interest and no methods of accounting can change that.”⁶⁵

convert what is interest into capital, this would afford an easy way to circumvent the *in duplum* rule. When interest is compounded it remains interest.⁶⁷

3.2. SALIENT DIFFERENCES IN APPLICATION OF THE *IN DUPLUM* RULE IN KENYA AND IN SOUTH AFRICA

3.2.1. WHAT COMPRISES THE AMOUNTS THAT OUGHT NOT TO EXCEED THE PRINCIPAL OWING AT THE TIME OF DEFAULT?

Kenyan legislation stipulates that the “...*principal owing when the loan becomes non-performing; interest, in accordance with the contract between the debtor and the institution, not exceeding the principal owing when the loan becomes non-performing; and expenses incurred in the recovery of any amounts owed by the debtor...*”⁶⁸ are what ought to be considered in determining the maximum amount recoverable by an institution from a debtor with respect to a non-performing loan.

The wording of this particular section begs for clarity as “...*any expenses incurred in the recovery of any amounts owed by the debtor...*” can be selectively and widely interpreted to encompass a wide array of ‘expenses’.

In the same light, South African legislation has a clearer position on the matter as it provides that

“*A credit agreement must not require payment by the consumer of any money or other consideration except*

(i) in the case of a credit facility, may be payable monthly, annually, on a per transaction basis or on a combination of periodic and transaction basis; or

(ii) in any other case, may be payable monthly or annually; and

(iii) must not exceed the prescribed amount relative to the principal debt;

(d) interest, which-

(i) must be expressed in percentage terms as an annual rate calculated in the prescribed manner; and

(ii) must not exceed the applicable maximum prescribed rate determined ...;

(e) cost of any credit insurance provided ...;

(f) default administration charges, which –

(i) may not exceed the prescribed maximum for the category of credit agreement concerned; and

(ii) may be imposed only if the consumer has defaulted on a payment obligation under the credit agreement, ...; and

(g) collection costs, which may not exceed the prescribed maximum for the category of credit

debt set out and also applies to the maximum default interest that may be charged on a specific credit agreement.⁷²

Lastly, the legislation even defines costs of credit insurance to include the credit insurance premiums payable on the permitted costs of credit insurance that may be charged.⁷³

This shows the stark difference in detail as regards the elements comprising the recoverable amounts under Kenyan legislation and its South African counterpart. The latter is much more detailed leaving little or no grey areas regarding its interpretation.

INVOLVING FINANCIAL INSTITUTIONS

It is of paramount importance to note that section 44A of the Banking Act clearly outlines the scope of application of the *in duplum* rule as only being applicable to loans involving institutions as seen from the wording of section 44A (1):

“An institution shall be limited in what it may recover from a debtor with respect to a *non-performing loan*...”⁷⁴

The Act further defines an institution to mean a bank or financial institution or a mortgage finance company⁷⁵ and describes a loan to include any advance, credit facility, financial guarantee or any other liability incurred on behalf of any person.⁷⁶ This has led to many positing that the introduction of the *in duplum* rule into the Kenyan legal framework was intended to govern the banking sector solely, thereby excluding its application from contracts between natural persons.⁷⁷

Conversely, South African jurisprudence provides an alternate view to the same. To begin with, the common law *in duplum* rule has been interpreted to not only relate to money lending transactions involving financial institutions but rather to all contracts where a capital amount that is subject to interest at a fixed rate is owed.⁷⁸ In *Sanlam Life Insurance Ltd v South African Breweries Ltd*⁷⁹ Bliden J said at 655D-I:

“[T]he *In Duplum* rule is confined to arrear interest and to arrear interest alone. In my judgment the reason for this is plain: it is to protect debtors from being

contracts where a capital amount that is subject to interest at a fixed rate is owing.” This was the position that was held in *LTA Construction Bpk v Administrateur, Transvaal*⁸² and was quoted in the *Ethekwini case*.

The South African position alludes to the fact that it would be utterly unfair and somewhat counterproductive to restrict the application of the rule to money lending transactions to which financial institutions are party to. This is because the objective of the rule is to protect debtors from exploitation. The object of protection of the law in this regard is the vulnerable consumer of credit that often finds himself bound by unfavourable credit terms and subsequently at the mercy of credit providers.

It ought to be duly noted that the Supreme Court of South Africa in the *Ethekwini case* was applying the common law *in duplum* rule and not the statutory *in duplum* rule. This is because the National Credit Act had not yet been passed into law hence the application of the common law *in duplum* rule.

The Kenyan position may, if not addressed, lead to a scenario where the only governing rules are that of the binding nature of a valid contract as has been expressed time and time again in local jurisprudence. “*A court of law cannot re-write a contract between the parties. The parties are bound by the terms of their contract, unless coercion, fraud or undue influence are pleaded and proved.*”⁸³ The same was also expressed in the case of *Housing Finance Co. of Kenya Limited v Gilbert Kibe Njuguna*⁸⁴ where it was held, “*Parties only bind themselves*

It is interesting to note that the *in duplum* rule cannot be waived by the debtor. This can be inferred from the public policy aspect upon which the enactment of the rule is based. Additionally, jurisprudence bears testimony to this as well and elaborates that the rule can neither be waived in advance nor during the lifetime of the credit agreement between the creditor and the debtor.⁸⁶

4.2. APPLICATION OF THE *IN DUPLUM* RULE TO JUDGEMENT DEBTS

The position taken by Kenyan legislation on the application of the *in duplum* rule to judgment debts may prove to be detrimental to the success in achieving the objective for which the rule was enacted into law. Under the Banking Act, section 44A is clear on whether or not judgment debts fall under its scope of application:

*“This section shall not apply to limit any interest under a court order accruing after the order is made”*⁸⁷

The logical deduction that can be made in this instance is that the interest on a judgment debt can accrue such as to surpass the original judgment debt. This appears to be an instance in which the codification of the rule seems to contradict its very essence embodied in the common law rendition of the rule.

The Civil Procedure Act provides as follows:

(1) Where and in so far as a decree is for the payment of money, the court may, in the

*such aggregate sum as aforesaid from the date of the decree to the date of payment or other earlier date, the court shall be deemed to have ordered interest at 6 per cent per annum.*⁸⁸

Interestingly, the position of some courts is that interest ought to begin running anew.. Upon judgment being given, interest on the full amount of the judgment debt commences to run afresh but will once again cease to accrue when it reaches the amount of the judgment debt, being the capital and interest thereon for which cause of action was instituted. This may be seen to be due to the perceived novation of the initial debt owed. This was the position held in *Commercial Bank of Zimbabwe v MM Builders and Suppliers PVT Ltd.*⁸⁹

Another issue requiring utmost concern is whether or not interest continues to accrue such as to surpass the principal amount being sued for during the litigation process before the judgment is made. Section 44A (4) remains mute on this pertinent question as it only addresses itself to judgment debts – the judgment has already been issued by the court.

As aptly pointed out by Khaseke,⁹⁰ when faced with this question the Supreme Court of South Africa observed that it was paramount to reiterate the purpose for the establishment of the *in duplum* rule in order to adequately answer the question of interest *pendente lite*.

“It appears as previously pointed out that the rule is concerned with public interest and protects borrowers from exploitation by lenders who permit interest to accumulate. If that is so, I fail to see how a creditor who has instituted action can be

thus justified. It is important to underscore that the clock is said to begin running from the time of service of the initiating process of the suit.

This position was disputed in a dissenting opinion issued by Madlanga J in the case of *Paulsen and Another v Slip Knot Investments 777 (Pty) Ltd*⁹² where he went on to find that the *in duplum* rule ought to be applicable during the litigation process. In doing so he thus reversed the contrary decision of the South African Supreme Court of Appeal in the *Standard Bank case*⁹³ because it ignored the debtor's right of access to courts and other valid policy considerations and, in doing so, failed to conduct a proper balancing exercise. This rendered it inappropriate for a court to make a choice one way or the other.⁹⁴ However, this was a dissenting opinion and thus, did not form part of the main judgment to which 5 of the judges concurred.

It is reasonable, therefore, to assume that the same argument would be lifted as it is and applied in the Kenyan context *mutatis mutandi*. The power of the courts to make an interim award in anticipation of the judgment to be issued alludes to the likelihood of application of the principle regarding interest pending litigation emanating from the *Standard Bank case*.

The application of the rule in the *Standard Bank case* is contentious. Although it is true that the delays, if any, in the litigation process are not the fault of the creditor, failure to apply the *in duplum* rule in this regard is in fact a burden that the debtor is forced to bear. The debtor is no longer afforded the protection of the *in duplum* rule due to the mere lack of expediency on

based on compound interest. It is in the interest of the government to have such penalties as it allows for efficient financial planning for the government based on consistent source of income; taxpayers' money.⁹⁷

There have been debates as to whether the *in duplum* rule ought to apply to such debts. An argument that may be advanced in furtherance of the application of the rule to tax debts is that failure to apply the rule will lead to taxpayers having to pay penalties that may accrue to more than the principle amount owed. This is because the penalties in this case often are subject to compound interest.

The application of the rule to tax debts can be refuted by the fact that the *in duplum* rule is meant to protect debtors from the exploitation of the creditors. This presupposes the contractual relationship between the borrower and the lender. Such a relationship is non-existent⁹⁸ between a taxpayer and the state, thereby excluding the application of the *in duplum* rule to tax debts.

However, a counterargument to this would be that generally, the practice of many jurisdictions is to object to increased or penalty interest on default.⁹⁹ An extrapolation of this practice and application in the realm of taxation ought to, reasonably, lead to its application

⁹⁵ The author chooses to focus on income tax as that is the form of tax most poorly remitted and is individual-focused as opposed to other forms of tax such as corporation tax or VAT which target legal rather than natural persons; the general subject of consumer protectionist laws such as the...

...the government is adequately compensated for the delayed taxes received.¹⁰¹ The penalty interest, in effect, serves to compensate the government for the opportunity lost – or rather delayed in the case of late remittance – that the government would have otherwise profited from. Simply put, the penalty interest ought to be proportional to the lost opportunity suffered by the government in this case.

In the Kenyan context, section 44A CAP 488 explicitly excludes the application of the *in duplum* rule from tax debts as it reads: “An institution shall be limited in what it may recover from a debtor with respect to a non-performing loan...”¹⁰² and further goes on to describe an “institution” to mean a bank or financial institution or a mortgage finance company.¹⁰³ The wording of the legislation consciously restricts the real realm of application of the rule to non-performing loans given by banks, financial institutions or mortgage finance companies.

The provisions of the Banking Act notwithstanding, the *in duplum* rule ought to be applied to tax debts as its failure to do so would leave the taxpayer in the exact same situation that Amendment No 9 of 2006 was meant to protect the consumer of credit from; exploitation by the creditor. Although in matters tax related the government does not afford credit to the taxpayer, though the taxpayer assumes the role of a debtor as he/she is obliged to pay the taxman just as a debtor has an obligation to his/her creditor.¹⁰⁴ Continuous accrual of penalty interest will lead to the debtor finding himself/herself in a bottomless pit of debt owed to the government.

compounded.¹⁰⁶

This seems to be a lacuna in consumer credit law that requires the application of the *in duplum* rule in order to prevent the exploitation of debtors in this regard. Further recommendations on the same will be extensively explored in the following chapter.

4.5. THE IMPLICATION OF TECHNOLOGICAL ADVANCEMENTS ON THE *IN DUPLUM* RULE

The Banking Act defines “loans” to include any advance, credit facility, financial guarantee or any other liability incurred on behalf of any person.¹⁰⁷ This thereby increases the scope of application of the rule to credit cards.

The application of the rule to credit cards is pertinent. Interest on credit card transactions accrues compound interest on a daily basis that commences on the date of the transaction.¹⁰⁸ Furthermore, penalty interest is charged on the outstanding amount owed every month and is subjected to compound interest. This means that with every late payment the nature of financial debt tends to become more and more insurmountable – a snowball effect.¹⁰⁹

Failure to apply the *in duplum* rule to such transactions would lead to a drastic increase in cases of personal bankruptcy as debtors would find themselves on the perpetual ascent of a mountain of debt whose gradient continuously becomes steeper.

¹⁰⁵ See generally Vessio ML ‘The Effects of the *In Duplum* Rule and Clause 103 (5) of the National Credit Bill 2005 on Interest’ Unpublished LLM Thesis, University of Pretoria, 2006.

measures to ensure its efficient, just and equitable application. Proportionate regulation ought to be applied to the rule. There are three pillars pivotal to this approach. Firstly, the rule ought to apply to all transactions involving an advancement of credit as opposed to maintaining the status quo which only allows for the rule's application to loans issued by financial institutions as defined by the Banking Act.¹¹⁰ This ought to ensure better consumer protection for debtors as advancements of credit or credit equivalents such as tax debts will fall under this category as well.

Secondly, the application of the rule during litigation is one that ought to be reviewed in line with the unhurried turn-around-time of the Kenyan courts.¹¹¹ Despite the argument that the application of the rule would be prejudicial towards the judgment creditor, failure to apply it – taking into consideration the sluggish pace at which civil disputes are resolved – would in fact be detrimental to the judgment debtor as he would be paying interest that he/she would otherwise have not paid. Perhaps a provision ought to be made for a period *pendente lite* during which the rule will be suspended and after such a period elapses, the rule may begin to apply.¹¹² This would be another avenue of applying pressure on the judicial system to resolve litigation disputes in a timely manner.

Robust regulation is lacking thereby hindering the optimal application of the rule. Section 44A (2) of the Banking Act ought to be expanded in order to provide clarity on the maximum amount an institution shall be limited in what it may recover from a debtor with respect to a non-performing loan. Clarity in this regard will have a twofold effect: protecting debtors

...is the fact that any contravention of the provisions of CAP 488 does not invalidate any contractual obligation between an institution and any other person.¹¹³ However, the same piece of legislation states that no institution is permitted to recover in any court of law interest and other charges which exceed the maximum permitted under the provisions of the Banking Act or the Central Bank of Kenya Act.¹¹⁴ The question that arises from such conflicting sections is whether the recovery of interest exceeding the principal owing at the time of default is valid if pursued outside a court of law.

Summarily, the inclusion of the aforementioned recommendations will lead to the fair and just treatment of both the creditor and the debtor. In the year 2000 Onyango-Otieno J. advocated, through the judgment issued in *Pelican Investment Ltd v National Bank of Kenya Ltd*,¹¹⁵ for the introduction of the *in duplum* rule in Kenya. The learned judge stated:

“...such a legal proposition might be ideal in this country as it will ensure that *debtors do not suffer the requirements upon them to pay extra-large interests caused by the indolence and lapse or deliberate failure by the creditors so as to let the unserviced loans accumulate interest to unimaginable levels. It will protect the debtors as well as ensuring that the creditors get their money back for further circulation and hence the economy will be healthy...*”

This is a goal worth pursuing and worthy of our each and every effort.

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