SAIPAR Case Review

Volume 5
Issue 1 *Special Edition in Honour of Chief Justice Mumba Malila (April 2022)*

Article 4

4-2022

Chrismar Hotel Ltd v Stanbic Bank Zambia Ltd SCZ Selected Judgment No 6 of 2017 p. 160

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Dunia P. Zongwe[4]

This case dramatizes the bank charges that most depositors are smacked with. Interest, overdraft charges, extension charges, restructuring fee, late charges, base rate, default interest, compound interest… In *Chrismar Hotel Ltd v Stanbic Bank Zambia Ltd*, Mumba Malila JS opened the judgment as follows:[5]

> Bank charges, especially those not expressly agreed to by customers, are increasingly becoming a worrisome consumer controversy in this country. Many a bank customer have quietly grumbled about what is viewed as unagreed debits on customers' accounts made up of variously labeled bank charges. This coupled with the seemingly unlimited authority of banks to do what they wish with customers' accounts in ensuring their profitability, has generated considerable resentment to some banking practices by consumers of banking services.

Apart from hinting at the eventual outcome, this opening soundbite captures both the core issues and the true significance of this case. More importantly, this case illustrates how bank charges can undermine freedom of contract – this sacrosanct principle of contract law and commercial law. Freedom of contract undergirds the market economy, as opposed to an economy ruled by command from above, the state. And two tenets of the Zambian legal system are precisely 'private initiative' and 'wealth' creation.[6]

Hopefully, Malila JS will carry over the keen sense of context and synthesis he displayed in *Chrismar Hotel* into the Constitutional Court that he now heads as Zambia's new Chief Justice. Though he did not extend this sense of context to society's economic dimensions in that judgment, the man who chairs the Constitutional Court will have a golden opportunity to shape fundamental questions and zoom in on their many aspects, not least of which the economy. To foreshadow such broader perspective, this commentary imagines how the court in *Chrismar Hotel* could have justified the outcome of that case had it weighed in on the consequences of heavy bank charges for commerce and society.

Facts

In the first semester of 2008, the appellant, Chrismar Hotel Ltd, needed finance to buy some equipment, including earth-moving equipment. It therefore solicited funds from the respondent bank, Stanbic Bank Zambia Ltd, with which it had held several accounts, obtained credit facilities (for example, mortgages and debentures), and established a longstanding relationship. The respondent bank agreed to lend money to the appellant hotel.

Thus, the hotel and the bank (hereinafter 'the parties') entered into eight distinct yet identically worded finance leases. For a total sum of 1.7 million US dollars, the eight leases each specified the amount that the respondent bank would finance together with the finance charges that the appellant should pay. The appellant secured the finance leases with third party mortgages over two properties.[7] In terms of the finance leases, the appellant had to repay the leased sums in

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[4] J.S.D. (Cornell); LL.M. (Cornell); Cert. (Univ. Montréal); LL.B. (Univ. Namibia); B.Juris (Univ. Namibia).

[5] *Chrismar Hotel Ltd v Stanbic Bank Zambia Ltd* SCZ Selected Judgment No 6 of 2017 p. 160 [J2] (hereinafter the '*Chrismar Hotel*' case).

[6] 1991 Constitution of Zambia, as amended by Act 2 of 2016, Art 10(1).

[7] A 'third party mortgage' arises where a third party (i.e., a person other than the debtor or the creditor) establishes a mortgage on his own property on the creditor's behalf as security for the debtor's debt. In a separate agreement with the creditor, the third party commits to the sale of his property under execution if the debtor fails to pay the debt for which the mortgage serves as collateral.

60 monthly installments ending on May 30th, 2013. By the time the lease ended, total repayment had to amount to 2,280,121.00 US dollars.

On December 4th, 2012, the appellant had paid back a total sum of 2,413,168.43 US dollars, but the respondent bank continued to apply a variety of charges and expenses with interest. The appellant therefore sued the respondent, complaining that the respondent breached the finance leases and the law. But, on May 23rd, 2016, except for the appellant's submissions on the value-added tax (VAT), the High Court dismissed the appellant's suit with costs. Thereupon, the hotel appealed against the High Court's ruling to the Supreme Court of Zambia.

The parties' arguments

In the Supreme Court, the appellant raised eight grounds of appeal. In summary, the appellant submitted that the High Court trial judge erred in law and in fact because:[8]

1. he held that the respondent hotel could overdraw the appellant's account although the parties never signed any overdraft agreement;
2. he failed to speak to the question whether, given that the respondent lacked the authority to transfer money from the appellant's Kwacha account to the Dollar account and vice versa, the transfers, overdraft, and interest charges the respondent made were illegal;
3. he held that the respondent could overdraw the appellant's account by way of standing orders[9] to cover the lease facility payments and still apply late charges, which ought to have been paid by the overdraft;
4. he held that, notwithstanding the fact that the finance leases did not provide for extension charges, the respondent could unilaterally apply those charges;
5. he failed to consider that, despite the restructuring fee that the respondent charged to the appellant in 2010 to reduce monthly installments to 25,000.00 US dollars, the respondent continued to charge interest on the monthly installments over and above the restructured amount;
6. he failed to address the discrepancy between the 336,066.32 US dollars charged to the appellant and the 188,435.08 US dollars explained by the respondent in its reconciliation, implying that the discrepancy reflected late charges or penal interest;
7. he held that Clause 2.4 intertwined with Clause 11.3 of the finance leases and that both relate to compound interest; and
8. he failed to find that the respondent charged late interest in addition to compound interest, which contravenes the Banking and Financial Services (Cost of Borrowing) Regulations[10].

Counsel for the appellant, State Counsel Mwansa and Ms. Findlay, astutely grouped these eight grounds of appeal into three clusters: one dealing with the overdraft (i.e., questions 1, 2, and 3), another with the extension charges (i.e., questions 4 and 5), and a third with the remaining issues compositely (i.e., questions 6, 7, and 8).[11]

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[8] *Chrismar Hotel* (n) [J8]-[J10].

[9] A standing order refers to the automated system whereby a person instructs its bank to pay another person a certain sum of money at regular intervals.

[10] Banking and Financial Services (Cost of Borrowing) Regulations, Statutory Instrument Number 179 of 1995 of the Laws of Zambia.

[11] See *Chrismar Hotel* (n)[J10].

Regarding the overdraft cluster, the appellant argued that it never authorized the respondent bank to create an overdraft facility, let alone impose charges on it.[12] Counsel insisted that the trial court erred in failing to recognize that the absence of evidence of any agreement or authority to transfer money between the appellant's accounts meant that the transfers violated the law.[13] Opposing the appellant's argument, counsel for the respondent, Mr. Mambwe, agreed with the trial judge's holding that there was no overdraft *per se* and that the impugned charges constituted overdraft charges.[14] To back up the trial court's holding and the respondent's argument that it had the right to overdraw and to charge for the overdraft, Mr. Mambwe mentioned the standing orders, the terms of the finance leases, and the fact that the appellant admitted having fallen into arrears.[15]

The appellant's lawyer submitted that, because the standing orders operated in respect of the appellant's Dollar account only, the respondent should not have overdrawn the Kwacha account on the basis of those standing orders.[16] Moreover, common Clauses 14 of the finance leases empowered the respondent to transfer money in any of the appellant's accounts towards the settlement of its debt, this clause did not authorize the respondent to debit the Kwacha account or any other account where that account had no money, and to thus create an overdraft.[17] Neither did it permit the respondent to charge interest of 36% to 37% on the overdraft.[18]

The appellant challenged the legality of the respondent's decision to charge compound interest. Specifically, the appellant reasoned that, if the respondent set up an overdraft facility to pay the lease accounts, this setup would prevent any possibility of default in the lease accounts, thereby precluding the need for any default or late charges.[19] The respondent retorted that, contrary to what the appellant affirmed, the trial court addressed the question of late charges when the court found that the respondent's right to charge the appellant for late payments was grounded in Clauses 2.4 and 11.3 of the finance leases.[20] Put another way, the finance leases entitled the respondent to charge compound interest on late payments and for the overdraft.[21]

Tackling the extension cluster, the appellant faulted the High Court for neglecting the fact that, although the respondent imposed in June 2010 a restructuring fee and charged the appellant to cut monthly installments down to 25,000 US dollars, the respondent kept on charging interest on installments over and above the restructured payment amount.[22] The respondent had claimed it levied the restructuring fee ('extension charges') because the base rate changed in 2008 from 10% to 12%,[23] the parties reduced the monthly repayments, the appellant benefited and asked for the restructuring, and Clause 17 of finance leases provided for the fee.[24] But the appellant insisted that the extension charges never formed part of its agreement with the

[12] *Chrismar Hotel* (n) [J10]-[J11].
[13] *Chrismar Hotel* (n) [J11]-[J13].
[14] *Chrismar Hotel* (n) [J25].
[15] *Chrismar Hotel* (n) [J25]-[J27], and [J13].
[16] *Chrismar Hotel* (n) [J13]-[J14].
[17] *Chrismar Hotel* (n) [J14]-[J15].
[18] See *Chrismar Hotel* (n) [J15].
[19] *Chrismar Hotel* (n) [J15]-[J16].
[20] *Chrismar Hotel* (n) [J27].
[21] *Chrismar Hotel* (n) [J27].
[22] *Chrismar Hotel* (n) [J14]-[J15].
[23] See *Chrismar Hotel* (n) [J45]. Set by the central bank, the base rate is the minimum rate at which banks can lend to their customers. The law prohibits banks from lending below that minimum rate.
[24] See *Chrismar Hotel* (n) [J19] and [J26]-[J28].

respondent, nor did anyone adduce evidence that the parties agreed on such charges or that the respondent expressly notified the appellant of the charges.[25]

The appellant maintained that, after it paid the fee of 85,809.40 US dollars to restructure monthly repayments from 39,000 US dollars to 25,000 US dollars, the respondent continued to charge the appellant the initial monthly repayment rate.[26]

With respect to the third cluster, the appellant submitted that the respondent bank made several errors. Among others, the respondent failed to explain why it imposed bank charges higher than the amount that the bank had itself arrived at when it did the reconciliation.[27] The appellant deemed the gap between the two amounts as revealing late charges and penal interest.[28] In addition, the respondent erred in finding that Clause 2.4 and Clause 11.3 of the finance leases both related to compound interest and that the late charges were penal in nature.[29] In particular, the appellant pointed out that, though the finance leases obliged the respondent to 'compound' default interest,[30] the 'default interest' applied by the respondent differed from 'compound interest'.[31] The respondent applied default interest over and above compound interest.[32] Insofar as it added an extra 10% to the base rate of 10%, that 'default interest' differed from compound interest and amounted to a punitive interest, which Zambian law forbids.[33]

The respondent denied that the High Court had blundered.[34] Regarding the numerical discrepancies, the respondent countered that the trial judge did not err in ruling in the bank's favor because what mattered was the principle on the basis of which the respondent imposed charges, not the actual figures of those charges.[35] The respondent also submitted that the appellant misinterpreted the terms of the finance leases, that Zambian banking law[36] allowed financial institutions to charge interest on overdue payments, and that therefore such interest did not equate to punitive interest.[37]

The court's rulings

After examining the parties' submissions and hearing the oral arguments and clarifications, the Supreme Court ruled on each of the eight grounds that the appellant leveled, and that the respondent oppugned. Delivering the judgment of the unanimous court, Malila JS ruled for the appealing hotel on six of the eight grounds.

Starting with the overdraft cluster, Malila JS found that, because no evidence could prove that the parties agreed to establish an overdraft, the respondent could not overdraw the appellant's Kwacha account.[38] Though the common law entitles a bank to combine a customer's accounts to settle his debts, a bank cannot exercise that right when an account does not have a credit and where the parties have not otherwise dealt with the delinquent account by, for example,

[25] *Chrismar Hotel* (n) [J19].
[26] *Chrismar Hotel* (n) [J19] and [J20].
[27] *Chrismar Hotel* (n) [J21].
[28] *Chrismar Hotel* (n) [J21].
[29] *Chrismar Hotel* (n) [J22].
[30] Clause 11.3, read together In Clause 2.4, of the finance leases.
[31] *Chrismar Hotel* (n) [J22]-[J23].
[32] *Chrismar Hotel* (n) [J22]-[J23].
[33] *Chrismar Hotel* (n) [J23]-[J24]. Counsel for the appellant cited Regulation 10(1) of the Banking and Financial Services Act (Cost of Borrowing) Regulation to buttress his submission that Zambian law forbids penal interest.
[34] *Chrismar Hotel* (n) [J29]-[J30].
[35] *Chrismar Hotel* (n) [J29].
[36] Banking and Financial Services Act (Cost of Borrowing) Regulation, Regulation 10(1).
[37] *Chrismar Hotel* (n) [J29].
[38] *Chrismar Hotel* (n) [J39]-[J40].

charging default interest.[39] Malila JS also accepted the appellant's argument that, since the respondent overdrew the appellant's Kwacha account, the overdraft obviated the need for the respondent to apply default and late charges.[40]

In settling the extension cluster, the learned judge ruled that the respondent acted unlawfully when it levied the restructuring fee without discussing it across the table and agreeing with the appellant on that fee.[41] Varying the finance leases in this manner without the appellant's consent would breach Clause 17.1 of the leases, which obliges both parties to reduce such variation in writing and to sign the variation.[42] For that reason, Malila JS observed that "the respondent acted outside the banker customer relationship and the contractual provisions contained in the lease agreements."[43] Further noting that the appellant never got value for the restructuring fee that it paid (since the respondent never restructured the monthly payments), the Supreme Court denounced the fee as "an extortionist charge".[44]

While broaching the composite cluster, Malila JS dissented from the High Court judge's position that the discrepancy between the extension charges actually paid and those declared during reconciliation.[45] Malila said that the disparate figures played a decisive role, for otherwise the Supreme Court would not have managed to assess the veracity of the stories that the parties told the Court.[46]

However, Malila JS set aside the remaining two grounds of appeal because he determined that the terms of the finance leases clearly allowed the respondent to charge compound interest.[47] He found that Clause 2.4 and Clause 11.3 of the leases complemented each other: Clause 2.4 of the leases *generally* stated that the respondent could charge interest on arrears while Clause 11.3 *specified* the rate of interest (i.e., 10% per year).[48] Hence Clause 11.3 did not introduce any new penal interest.[49]

In the end, the Supreme Court upheld the appellant's appeal. Because the respondent created an overdraft facility without the appellant's consent, the court ordered that the overdraft cover charges be reversed.[50] And, given the overall outcome of the case, the court ordered the respondent bank to pay the costs.[51]

Significance of the case

By demonstrating Malila's ability to drill down to the essential components of complex finance disputes, this case takes on a starker relief, especially after President Hakainde Hichilema appointed and sworn in Malila as Zambia's Chief Justice.[52] The highly technical points that

[39] *Chrismar Hotel* (n) [J39]-[J42].
[40] *Chrismar Hotel* (n) [J42]-[J43].
[41] *Chrismar Hotel* (n) [J45].
[42] *Chrismar Hotel* (n) [J45]-[J46]. On several occasions, counsel for the appellant drew the court's attention to Clause 17 of the finance leases, which provided for non-variation and indulgence. See *Chrismar Hotel* (n) [J15] and [J19]-[J20].
[43] *Chrismar Hotel* (n) [J47].
[44] *Chrismar Hotel* (n) [J49].
[45] *Chrismar Hotel* (n) [J49]-[J50].
[46] *Chrismar Hotel* (n) [J49]-[J50].
[47] See *Chrismar Hotel* (n) [J50]-[J52].
[48] *Chrismar Hotel* (n) [J51].
[49] *Chrismar Hotel* (n) [J52].
[50] *Chrismar Hotel* (n) [J52].
[51] *Chrismar Hotel* (n) [J54].
[52] President Hakainde Hichilema appointed Malila as Zambia's Chief Justice on 17 November 2021 and sworn him into office on 22 December 2021.

these disputes bring up call for consummate analytical skills, which will then enable the new Chief Justice to tackle the constitutional aspects of disputes about finances.

Aside from this, the *Chrismar Hotel* case does raise concerns about consumer protection. Indeed, the bank charges that depositors often encounter without knowing what warrants them are precisely the circumstances that prompted jurisdictions like South Africa to institute the Financial Sector Conduct Authority. Malila JS appears to recognize the necessity to protect consumers and stop unprincipled banks from taking advantage of the less financially savvy. He deplored the "hugely unfair" attitude of the respondent who fashioned bank charges so as to maximize profit "at the expense of the appellant" and who let the charges "snowball out of control":[53]

> There is no doubt whatsoever that the respondent bank in the circumstances as described utilised the inability of the appellant to be current on its lease repayments to curve out maximum profitability for itself. If the respondent bank had considered, even for a moment, the financial interests of the appellant, the creation of the overdraft facility and the charging of overdraft charges and default interest at the same time, should not have occurred.

The unanimous court somewhat remedied Chrismar Hotel's bank charges, still it has not resolved this issue for the rest of bank depositors, most of whom do not understand the nitty-gritty of those charges – a situation that threatens financial inclusion. Obviously, the appellant hotel has more financial resources and sophistication than ordinary bank customers. For that reason, a durable solution to multi-faceted bank charges calls for something more than just a law prohibiting penal charges, more than just a court judgment that forbids such charges.

Conclusion

Chrismar Hotel has demonstrated Malila CJ's analysis and synthesis of intricate finance disagreements. These skills manifested, for example, when Malila determined that the whole overdraft question hinged on whether the parties had, in fact, agreed on an overdraft facility. In doing so, he distinguished between a loan and an overdraft.[54] The learned judge did not explain why this dichotomy mattered, but the dichotomy decides the whole overdraft question because a loan, as evidenced by the parties' finance leases, does not automatically entail an overdraft: The parties must conclude a separate, distinct agreement to establish an overdraft facility. This acute sense of analysis, synthesis and significance will serve Malila CJ in the Constitutional Court when adjudicating on commercial law disputes, though he will only be expected to approach those disputes from a constitutional perspective.

Even from that perspective, the *Chrismar Hotel* case drew forth conundrums whose resolution requires a firm grasp of the Constitution. These issues notably feature freedom of contract. Indeed, freedom of contract underlies the market economy. In this respect, it is a 'constitutional' principle of the Zambian legal system. Article 10(1) of the Constitution obliges the government to "create an economic environment which encourages *individual initiative*…

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[53] *Chrismar Hotel* (n) [J43].

[54] *Chrismar Hotel* (n) [J30]-[J31]. Malila JS distinguished these two credit agreements as follows: A 'loan' denotes a special arrangement whereby a bank advances to a customer a specified, definite amount of money. The customer may withdraw the approved amount at once, in which case the bank debits the amount against the customer's account. By contrast, a customer uses and enjoys an 'overdraft' gradually as needs arise, up to the maximum amount approved by the bank. Unlike a loan, an overdraft facility does not require that the customer reaches the limit of the sum approved by the bank.

so as to promote investment, employment and *wealth*."[55] *Chrismar Hotel* teaches depositors and policymakers this lesson: Complex bank charges may end up breaching the bank-customer relationship. More generally, *complex bank charges may subvert freedom of contract*. Future litigation before the Constitutional Court will afford the new Chief Justice opportunities to delve more deeply into and expound on the freedom-of-contract principle to ensure that the entire banking system caters to the needs of customers, and not simply the profit-maximizing goals of capital owners.

Had it systematically factored in commerce and the economy, how would the Supreme Court have approached *Chrismar Hotel?* This case shows that, while overdraft facilities generate more profits than loans,[56] the respondent accepted to extend a loan rather than insisting on an overdraft. Not only would the overdraft have avoided the default and late charges that the appellant incurred, but it would also have avoided the costs of this litigation. With an overdraft, the parties could have even prevented the restructuring fee, depending on the limit of the overdraft. This implies that the parties poorly designed their agreement. They should have structured their agreement as an overdraft from the start.

Crucially, the parties should not have empowered the respondent to charge default interest on the base rate. Malila JS mistakenly construed Clause 2.4 and Clause 11.3 of the leases because they do not follow the mathematical formula for compound interest.[57] Moreover, lenders typically calculate compound interest based on the principal or the interest accumulated over the past time periods, and not based on a base rate. Malila JS should have ruled – like the appellant invited him to do – that the default interest, though not necessarily punitive, differed from compound interest. The devil in the detail of finance disputes can elude even eagle-eyed analysts as seasoned and skilled as the new Chief Justice.

[55] 1991 Constitution of Zambia, as amended by Act 2 of 2016. Emphasis added. Article 10 is entitled "Basis of economic policies".

[56] The respondent charged 36% to 37% on the overdraft. See *Chrismar Hotel* (n) [J15].

[57] The mathematical formula for compound interest looks like this: $A = P(1 + r/n)(nt)$, where *P* stands for the principal balance, *r* for the interest rate, *n* for the number of times interest is compounded per time period, and *t* for the number of time periods.