

THE REPUBLIC OF UGANDA
IN THE COURT OF APPEAL OF UGANDA AT KAMPALA
CIVIL APPEAL NO. 80 OF 2015

(CORAM: R. Buteera, DCJ; C. Bamugemereire & S. Musota, JJA)

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UAP INSURANCE UGANDA LTD APPELLANT

VERSUS

NATIONAL HOUSING & CONSTRUCTION CO. LTD..... RESPONDENT

10 *(An Appeal arising from the Ruling and orders of the High Court (Commercial Division) before B. Kainamura, J, dated 18th November 2013 in Miscellaneous Application No. 684 of 2013 arising from Civil Suit No. 427 of 2013)*

JUDGMENT OF BUTEERA, DCJ

Introduction

15 This is an appeal by UAP Insurance Uganda Limited (the appellant) from the decision of the High Court (Commercial Division) delivered by B. Kainamura, J, on 18th November 2013 by which the appellant was ordered to pay a sum of USD 1, 813, 881 (United States Dollars One Million Eight Hundred Thirteen Thousand Eight Hundred Eighty-One) plus costs. Ruling was entered by the
20 learned Judge after hearing the appellant's application for unconditional leave to appear and defend brought under Order 36 rule 4 of the Civil Procedure Rules.

Background

25 The background to this Appeal is that on 15th July 2011, National Housing and Construction Company Limited (the respondent) entered into an agreement ('the Head Contract') with NH-MKP Builders Limited (NH-MKP) for the construction of condominium apartments in Naalya at a contract price of USD

18, 138, 812 (United States Dollars Eighteen Million One Hundred Thirty-Eight Thousand Eight Hundred and Twelve).

On 22nd July 2011, NH-MKP Builders Ltd entered a sub- contract for the construction of the aforesaid apartments with M/S MKP Builders SDN BHD (MKP) the nominated sub- contractor in the Main Contract. Pursuant to clause 2 of the Main Contract, M/S NH-MKP Builders Ltd was required to obtain a Performance Bond in favor of the respondent as security for compliance with its obligations in the contract.

On 11th November 2011, M/S NH- MKP Builders Ltd executed a Performance Bond No. 101/ 132/ 1/ 000685/ 2011 with the applicant in favour of the respondent wherein it was agreed that the appellant shall pay a sum of USD 1, 813, 881 (United States Dollars One Million Eight Hundred Thirteen Thousand Eight Hundred Eighty-One) to the respondent upon demand without the respondent needing to prove or show grounds or reasons for its demand for the sum specified.

The Performance Bond was tenable up to 17th April, 2013. On 4th February 2013, the respondent made a demand on the applicant and after a series of correspondence, on 24th April 2013, the appellant communicated to the respondent that it was not liable on the Performance Bond. The respondent then filed High Court Civil Suit No. 427 of 2013 by summary procedure seeking the recovery of the sums secured by the Bond. The appellant filed an application for leave to appear and defend, arguing that the Bond and the demand were vitiated by fraud and illegality. The application was rejected and court entered judgment in favour of the respondent, hence this appeal.

Grounds of Appeal

The grounds of appeal were stated in the Memorandum of Appeal as follows:

1. The learned trial Judge erred in law and fact in holding that there were no triable issues raised by the appellant.

2. The learned trial Judge having observed that the main issue was whether the guarantee was riddled with fraud erred in law in;

a) Failing to grant the appellant leave so that the issue could be tried on its merits.

b) Proceeding to make a finding on the issue without according the appellant an opportunity to lead evidence on the matter.

Orders sought

The appellant sought for orders that:

1. The appeal be allowed.

2. The Judgment and orders of the High Court in Miscellaneous Application No. 427 of 2013 be set aside and substituted with an order granting the appellant unconditional leave to appear and defend the suit.

3. Costs be provided for in this Court and in the High Court.

Representation

At the hearing of the appeal, the appellant was represented by Mr. Joseph Luswata and Ms Josephine Muhaise, while the respondent was represented by Mr. Isaac Walukagga.

Both counsel filed written submissions and applied to court to adopt them as their arguments. This application was granted. These submissions have been relied upon in this Appeal.

Ground 1

Case for the appellant

Performance bonds

Counsel for the appellant submitted that a performance bond is one example of a guarantee and it is a binding contractual undertaking given by a person (usually Bank or Insurance company) to pay a specified amount of money to

a named beneficiary on the occurrence of a certain event which is usually the non- fulfilment of a contractual obligation.

Citing Hudson's Building and Engineering Contracts (Twelfth Edition) page 1317- 1318, he stated that in the context of construction contracts, as in this case, a performance bond is issued to secure the performance of a contractor's obligations under a construction contract. That the guarantor (usually an insurance company) undertakes to pay a specified amount to the beneficiary in the event that the contractor fails to perform its obligations under the construction contract. It was counsel's view that a performance bond has three parties namely, the contractor who applies for the bond, the insurance company which issues the bond and the client who is the beneficiary of the bond.

He submitted further that a performance bond is also called a demand guarantee if by its terms it is payable on demand. He cited **Bradford Old Bank v Sutcliffe (1918) 2 KB 833** or **Re Browns Estate (1893) 2 Ch 300** and contended that '*payable on demand*' means that liability to pay arises on a mere demand by the beneficiary, even if there is a reason to doubt that the primary obligation has been broken.

Counsel submitted that it is well established that if the beneficiary seeks payment in accordance with the terms of the bond, the guarantor of the bond must pay, regardless of how unfair that might be to the contractor or regardless of any justification which might exist for non- performance. He cited **Edward Owen Engineering Ltd v Barclays Bank International Ltd (1978) QB 159**, that was relied upon by the Court of Appeal of Uganda in **Trans Africa Assurance Co. v Cambria (1997- 2001) UCLR**.

In counsel's view, that embodied the concept of 'autonomy' to the effect that the bond is a separate contract from the underlying contract and therefore issues of disputes between the parties in the contract whose performance has

been guaranteed (the underlying contract) do not affect the enforcement of the bond by the beneficiary.

He stated that performance bonds have been treated as analogous to letters of credit, and therefore as being the same as promissory notes payable on demand, bills of exchange or cash giving rise to the concept of '*cash principle*' or '*pay and argue later*'.

Counsel argued that a misrepresentation of a material part of the transaction by a beneficiary or with the beneficiary's knowledge voids a guarantee. He referred to Section 83 of the Contracts Act, 2010, which provides as follows:

10 "A guarantee which is obtained by a misrepresentation made by a creditor or with the knowledge and assent of a creditor, concerning a material part of the transaction is void."

'Creditor' is defined in Section 68 of the Contracts Act to mean a person to whom a guarantee is given.

15 **Principles governing leave to appear and defend**

Counsel submitted that an applicant must demonstrate to court by affidavit evidence that there is an issue or question of fact or law which is in dispute. He referred to **Odgers Principles at page 71**. He noted that the issue must be bonafide, citing **Maluku Interglobal Agency Ltd v Bank of Uganda (1985) HCB 65**. He further noted that it must be a genuine or plausible defence either of fact or of law, citing **Abubaker Kato Kasule v Tomson Muhwezi (1992-93) HCB 212**. Counsel further stated that the facts pleaded must lead to an inference that at the trial of the action, the applicant may be able to establish a defense to the claim. He referred to **Provincial Insurance Co. of East Africa v Kivutu (1995- 98) 1 EA 283 at 285**.

Counsel submitted that the standard of proof of whether a triable issue has been established is on a balance of probability. He argued that where the suit is on a repudiation of a performance bond, the issue of fact or law or the

triable issue must be any or both namely: that the bond was issued in error or is vitiated by fraud or misrepresentation. This is because these are the only defenses against a demand on a performance bond recognizable in law available to the guarantor of a bond. He referred to the persuasive authority
5 of **AC Yafeng Construction Limited v The Registered Trustees of Living Word Assembly Church & Anor; Civil Miscellaneous Application No. 1 of 2021.**

He pointed out that the issue in this case was whether the appellant raised any triable issues of law or fact warranting the grant of leave to the appellant
10 to defend the suit. He noted that the trial Judge in his Ruling stated:

*“As borne out in the affidavits and submissions on record, the triable issues are the status and enforceability of the Performance Guarantee issued under the Head Contract viewed alongside the provisions of and as impacted by the Sub- Contract. Of particular
15 relevance is whether the demand on the Performance Bond is vitiated by fraud.”*

Counsel submitted that despite correctly pointing out the triable issues, the trial Judge went ahead to determine the issues identified without a trial. He contended that the trial Judge raised the standard of proof of the existence
20 of triable issues higher than on a balance of probability. He contended further that the trial Judge erred, having identified the triable issues, to go ahead to resolve them summarily without affording the appellant an opportunity to defend itself. He referred to **Children of Africa v Sarick Construction Limited MA 134 of 2016**, a persuasive authority of the High Court sitting at
25 Gulu.

It was counsel's further submission that the issues of fact that warrant trial are:

1. Did NH- MKP assign its obligation to implement the Head Contract to MKP?

2. Whether it was NH- MKP or MKP that was obligated to construct the Naalya Pride Project.

3. Did the respondent have knowledge of the assignment and MKP's obligations?

4. Whether the appellant issued the performance bond with the knowledge that NH-MKP had assigned its obligations under the Head Contract to MKP.

5. Whether the respondent was privy to or had notice of the representation made by NH- MKP that it was constructing the Naalya Pride Project.

6. Whether it was NH- MKP or MKP that failed to perform the contract for construction of the Naalya Pride Project

7. Did the respondent issue the demand to the appellant with knowledge that MKP was implementing the Naalya Pride Project?

8. Whether MKP obtained a performance security from Lion Assurance in respect of the construction of the Naalya Pride Project.

Counsel further submitted that the issues of law that arose from the questions of fact were:

1. Whether the subcontract between NH- MKP and MKP amounted to a novation/ assignment or was a subcontract only. If it was a novation, who would be the right party to take out the performance bond.

2. Put differently, what is the effect of clause 6 of the subcontract agreement which provides that '*for all intents and purposes, the subcontractor shall assume the responsibilities and liabilities of the Contractor as provided in the Naalya Pride Construction contract dated 15th July...*' or the effect of clauses 3 and 5 of the subcontract agreement which require the subcontractor to obtain performance security for the benefit of the respondent.

3. In the circumstances where the performance bond was taken out by a party who was not performing the contract, is the appellant liable on the bond.

4. Can the nonperformance by MKP be a lawful ground to call on a guarantee issued to NH- MKP?

5. What is the effect of any misrepresentation committed with the knowledge of the respondent on the validity of the bond?

6. Does it amount to fraud for the respondent to call on a bond issued to NH- MKP when the default in performance is by another person.

10 It was counsel's submission that the above issues of law and fact were genuine, bonafide and not a sham and the trial judge should have allowed the appellant to defend the suit. He contended that, instead, the learned trial judge held that it was perfectly legal to create special purpose entities or vehicles for projects of the nature of Naalya Pride Project and that the Head
15 Contract provided for MKP as a subcontractor.

Counsel cited the case of **Solo Industries UK Limited v Canara Bank** (supra) to argue that a defendant who has raised evidence that the demand on a bond may be fraudulent should be allowed to defend the case.

He prayed that the Appeal be allowed and the appellant be allowed to file a
20 defence. He also prayed for costs of the Appeal.

Case for the respondent

Counsel for the respondent referred to the Judgment of the High Court where the trial Judge held that the appellant was liable to pay the respondent since the Performance Bond was not vitiated by fraud as alleged by the appellant.

25 Regarding the appellant's contention that the trial Judge ought to have granted the appellant leave to defend the suit when he noted that the main issue was whether the respondent had been fraudulent, counsel argued that the bar was a little higher than that as asserted by the appellant. He submitted

that the applicant must while alleging fraud raise triable issues that speak to the fraud complained of and this must be attributable to the respondent. That in this case, the appellant did not demonstrate any bad faith or dishonesty on the part of the respondent. He cited the persuasive authority of **Bosley Fredrick & Mohammed Ali t/a Continental Traders & Marketing v Westmount Power (Kenya) Limited; Kenya High Court Civil Suit No. 1700 of 2001.**

Regarding the alleged fraud by the respondent, counsel submitted that the appellant was at all material times aware that NH- MKP was required to secure a Performance Bond in favor of the respondent and that the contract was to be sub- contracted to MKP. It was his contention, therefore, that the demand to make good on an irrevocable bond by the respondent was therefore honest and not in any way fraudulent as argued by the appellant.

Regarding whether the Bond was issued under the Head Contract or the subcontract, counsel contended that the Head Contract to which NH-MKP was a party was the only contract that called for a Performance Bond. That the subcontract did not come into issue at all.

He argued that the Head Contract was to be performed by NH- MKP while the subcontract was to be performed by MKP and that it was NH- MKP that failed to perform its obligations.

He submitted that there were therefore no triable issues in the above arguments. He prayed that the Appeal be dismissed with costs in this Court and the court below. He also prayed for interest at commercial rate from the date of Judgment till payment in full.

Court's consideration of the Appeal

In the instant Appeal, whereas counsel for both parties dwelt at great length on the substance of the Head Contract and the subcontract, the gist of this appeal is whether the appellant's application for leave to appear and defend the summary suit in High Court Civil Suit No. 427 of 2013, met the requirements for grant of such an application. And whether, in rejecting the Application, the learned trial Judge erred.

Order 36 of the CPR provides for summary procedure on a specially endorsed plaint. Rule 3 provides for applications for leave to appear and defend as follows:

3. Judgment in default of application for leave to defend.

(1) Upon the filing of an endorsed plaint and an affidavit as is provided in rule 2 of this Order, the court shall cause to be served upon the defendant a summons in Form 4 of Appendix A of these Rules, or in such other form as may be prescribed, and the defendant shall not appear and defend the suit except upon applying for and obtaining leave from the court.

It is trite that summary procedure was designed to serve a purpose. In **Post Bank (U) Limited v Abdul Kasozi**; SCCA No. 08 of 2015; the Supreme Court stated thus:

“Order 36 was enacted to facilitate the expeditious disposal of cases involving debts and contracts of a commercial nature to prevent defendants from presenting frivolous or vexatious defences in order to unreasonably prolong litigation. Apart from assisting the courts in disposing of cases expeditiously, order 36 also helps the economy by removing unnecessary obstruction in financial or commercial dealings.”

Courts have set down the law that governs applications for leave to appear and defend. In **Kotecha vs Mohammed [2002] EA 112**, Court stated that:

5 **“where a suit is brought under summary procedure on a specially endorsed plaint, the defendant is granted leave to appear and defend if he was able to show that he had a good defence on merit, or that there is a difficult point of law involved, or a dispute as to the facts which ought to be tried, or a real dispute as to the amount claimed which required taking into account to determine; or any other circumstances**
10 **showing reasonable grounds of bonafide defence.”**

Bearing in mind the purpose of summary procedure, it is important to balance the need to expeditiously dispose of commercial cases with that of ensuring that a party that has adduced evidence to show that there are triable issues or that they have a good defense is not locked out. Fortunately, in cases where
15 court may have some doubt as to the strength or veracity of the proposed defense, it may proceed to grant conditional leave. The essence is that a person is not denied the all- important need of being heard.

In this case, the learned trial Judge while determining the appellant’s application for leave to appear and defend, made the following observation
20 on page 9:

*“As borne out in the affidavits and submissions on record, the triable issues are the status and enforceability of the Performance Guarantee issued under the Head Contract viewed alongside the provisions of and as impacted by the Sub- Contract. Of particular
25 relevance is whether the demand on the Performance Bond is vitiated by fraud.”*

Having so found and ably identified the triable issues, the learned trial Judge went ahead to resolve those issues. On page 10, he stated as follows:

5 *"I will first deal with the contention by Learned Counsel for the applicant that since NH- MKP had substantially sub contracted the building of the apartments to MKP then the Head Contract that required NH- MKP to provide the Guarantee had been overtaken by events and subsumed in the sub- contract, and that in fact the Head Contract was no longer in force. I respectfully disagree."*


10 It is my view that once court established that there were triable issues, the only option available to the learned trial Judge was to allow the application and give time to the appellant to file its defense so that the matter could be heard on merit. That did not happen.

15 It does not matter that the learned Judge may have correctly resolved the said issues. Doing so without permitting the appellant an opportunity to also adduce evidence and prove its case would amount to locking the appellant outside court. It equally does not matter that the triable issues may not eventually be decided in the applicant's favor. Ultimately, what is important is that a party is accorded the right to be heard.

20 For those reasons, I would allow the appeal, set aside the High Court Ruling, allow the application for leave to appeal and refer this matter back to the High Court so that the substance of the dispute between the appellant and the respondent is heard and determined on merit.

 Since the other two members of the Panel concur with my findings, it is therefore the unanimous decision of this Court that the Appeal succeeds. The respondent shall meet the costs of this Appeal and in the High Court.

25 Dated at Kampala this 15th day of Mar 2023


Richard Buteera
Deputy Chief Justice

THE REPUBLIC OF UGANDA
IN THE COURT OF APPEAL OF UGANDA AT KAMPALA
CIVIL APPEAL NO.80 OF 2015
(CORAM:BUTEERA, DCJ; BAMUGEMEREIRE & MUSOTA, JJA)

UAP INSURANCE UGANDA LIMITED ::::::::::::::: APPELLANTS

VERSUS

**NATIONAL HOUSING &
CONSTRUCTION CO. LTD :::::::::::::::RESPONDENT**
*(Arising out of the Ruling of Kainamura J, in Miscellaneous Application No. 684 of
2013 which arose out of
Civil suit No. 427 of 2013)*

JUDGMENT OF CATHERINE BAMUGEMEREIRE JA

I have had the privilege to read, in draft, the Judgment of my learned brother the Hon. Justice Richard Buteera DCJ. I am in agreement with his findings, conclusion and orders.

Dated this 15th day of March 2023



CATHERINE BAMUGEMEREIRE
JUSTICE OF APPEAL

THE REPUBLIC OF UGANDA
IN THE COURT OF APPEAL OF UGANDA AT KAMPALA
CIVIL APPEAL NO. 80 OF 2015

*(Arising from the ruling and orders of the High Court (Commercial Division
before Kainamura, J, in Misc. Application No. 684 of 2013)*

UAP INSURANCE UGANDA LTD ::::::::::::::::::::::::::::::::::: APPELLANT

VERSUS

NATIONAL HOUSING & CONSTRUCTION CO. LTD ::::::: RESPONDENT


CORAM: HON. JUSTICE RICHARD BUTEERA, JA
HON. JUSTICE CATHERINE BAMUGEMEREIRE, JA
HON JUSTICE STEPHEN MUSOTA, JA

JUDGMENT OF HON. JUSTICE STEPHEN MUSOTA, JA/JCC

I have the benefit of reading in draft the judgment by my brother Hon.
Justice Richard Buteera, DCJ.

I agree with his analysis, conclusions and the orders he has proposed.

Dated this 15th day of March 2023



Stephen Musota
JUSTICE OF APPEAL