THE REPUBLIC OF UGANDA

IN THE HIGH COURT OF UGANDA AT KAMPALA

HCT-00-CC-CI-0009-2005

IN THE MATTER OF THE COMPANIES ACT

AND

IN THE MATTER OF RANCH ON THE LAKE LIMITED (IN RECEIVERSHIP)

BEFORE: THE HONOURABLE MR. JUSTICE FMS EGONDA-NTENDE

RULING

1. Mr. Micheal Mawanda, hereinafter referred to as the Receiver, was appointed a Receiver by the Development Finance Company of Uganda Ltd, hereinafter referred to as the DFCU to liquidate Ranch on the Lake Limited, hereinafter referred to as the company, after the company defaulted in settling its indebtness to the DFCU and another secured creditor, East African Development Bank, hereinafter referred to as the Bank. The Receiver sold the security or securities, realising the sum of Shs.1,000,000,000.00 (One billion shillings) only.
2. The Receiver has come to this court seeking directions with regard to the disbursement of the proceeds, specifically in relation to two secured creditors, DFCU and the Bank, who have locked horns over the matter.
3. The brief background to this case in so far as may be relevent to the matters in issue are that both DFCU and the Bank advanced sums of money to the company all of which were secured by the same securities. As lenders DFCU and the Bank entered into a Security Sharing Agreement dated 16th September 1996 in which the lenders set out the terms that would govern their relationship. In due course the company failed to meet its obligations and both lenders tried cooperating with the company to find a buyer for its assets but this did not succeed.
4. On the 17th September 2001 DFCU appointed a Receiver relying on its powers as a mortgagee and the Bank was notified of this action on the same date. The Bank responded to this notification with its own letter calling upon DFCU to rescind its action,

and allow the sale of the securities to be conducted by the company with support from the lenders. DFCU did not alter its position on the appointment of a Receiver.

5. The Receiver subsequently sold the securities and realised a sum of Shs.1,000,000,000.00. After receipt of this sum of money the Receiver sought the directions of this court in this present application as to how to disburse the said amount as between DFCU and the Bank.
6. Before the Security Sharing Agreement, the position of the parties were that their individual interests in the said securities would rank pari passu to each other. Had the position remained as such no problems would have arisen. However, the Security Sharing Agreement introduced a further condition or term in the relationship of the parties with regard to realisation of securities which is the cause and or the crux of the current dispute. This is clause 4.2 which states,

> "The lenders agree that for purpose of enforcing any security, the entitlement of each lender to receive a share of such proceeds shall be dependent upon such lender having already enforced the security held by it or having taken and be actively pursuing steps to enforce the security held by it."

7. Relying on this provision the Receiver and DFCU argue that the Bank is not entitled to share in the proceeds of the sale of the securities as it did not enforce any security, nor did it actively take steps to enforce the security held by it, the first step of which would be to make a statutory demand. On the other hand, the Bank contends that this provision is void for inconsistency with the Section 11 of the Mortgage Act. Secondly the Bank contends that it took active steps to enforce the securities. Thirdly that it enforced this security by concurrance in conduct with the Receiver appointed by DFCU, in accordance with its agreement with the company.
8. It is convenient to set out Section 11 of the Mortgage Act at the outset. It states,

> "(1) The proceeds from any sale under this Act shall be applied as follows, and in the following order---
>
> (a) in payment of all expenses properly incurred or incidental to the sale or any prior attempted sale; (b) in payment of all sums due to the mortgagee and to any other encumbracer with the same order of priority; (c) in payment in the order of priority of any encumbracers subsquent to the

mortgagee; and (d) the residue, in any, in payment to the mortgagor."

9. Does Section 11 of the Mortgage Act void clause 4.2 of the Security Sharing Agreement as contended by the Bank? Ordinarily mortgages registered over the same property take priority as between the mortgagees according to the dates such mortgages were entered on the register in accordance with Section 48 (1) of the Registration of Titles Act. However, parties holding the same interest may agree to vary the order of priority as between themselves, as the parties here did both in Clause 3.1 of the Security Sharing Agreement, and in other instruments between them in which they agreeed that priority shall be pro rata and or pari passu their respective secured liability.
10. Section 11 of the Mortgage Act deals, in my view, with the order of priority, as between different classes of encumbrancers, and does not deal with priority of encumbracers within the same class of encumbrace. For that reason it cannot, in my view, void Clause 4.2 of the Security Sharing Agreement, as it would not void Clause 3.1 of the same agreement, or all the other provisions relating to priority as agreeed between the parties in other instruments between them.
11. For whatever reason the parties agreed to include Clause 4.2 in the Security Sharing Agreement. It established a condition precedent to participating in the proceeds of realisation of the security by one party. This condition was that the other party should already have 'enforced the security held by it or having taken and be actively pursuing steps to enforce the security held by it.' THE BANK contends that this clause is ambigous. The meaning of the same is fairly clear. If one party enforced the security the other party would only share in the proceeds, assuming that the proceeds are not sufficient to meet all secured liabilities and consquent costs, on a pro rata basis or pari passu basis, if that party had taken steps too to enforce its security, for instance as was provided for in clause 6 (a) of the Deed of Debenture between the company and the Bank dated 29th July 1996, and annexed to the affidavit of Mr. Onen of the East African Development Bank. This provided for concurrance with another person in selling the charged property.
12. It is in fact the contention of the Bank that it concurred in the sale of the securities, and is therefore entitled to share in the proceeds. For evidence of concurrance reliance is on

correspondence between the parties and or the Receiver. These are annextures V, W, X, Y, Z, AA, BB, CC, DD, FF, GG, HH, II, JJ, KK, LL, MM, NN, OO, PP,QQ, RR, SS, TT, UU, VV, and WW to the affidavit of Mr. Onen of the Bank.

13. I have carefully read the above letters and or correspondence between DFCU, the Bank and the Receiver. Annexture V is the first response of the Bank to the appointment of a Receiver of the company. The Bank in no uncertain terms in this letter did not concur in the appointmentof the Receiver. On the contrary it opposes this move, and requests that the appointment of a Receiver be rescinded, to allow a sale without Receivership. The subsquent correspondence is devoted, among other business, to ascertaining the the correct liability of the company to the Bank, but not expressly or even implicitly,touching upon the subject of exercise of the powers of concurrance provided for under Clause 6 (a) of the Debenture Agreement referred to above. It appears to me that an assumption was made by the Bank that it would automatically share in the proceeds, and on that basis proceeded in relating to the Receiver.
14. Prior to the appointment of a Receiver by DFCU, the parties had participated in joint efforts with the company, to sell the company or its assets, as a going concern, without enforcing their security. These efforts were unsuccessful. DFCU then embarked on enforcing the securities. The efforts prior to enforcement of the securities do not in my view amount to enforcement of a security or steps to enforcement of a security. To this end these efforts do not provide proof that the Bank took steps to enforce the security. On the contrary, these steps were intended to recover the sums outstanding, without enforcing the security, as it was thought, initially, that this would be the better business option. In effect this is the view of the Bank, expressed in its letter of 19th September 2001, Annexture V to Mr. Onen's affidavit.
15. For the foregoing reasons I am unable to find that the Bank took any steps to enforce its security so as to qualify in sharing in the proceeds realised from the eforcement of the security by DFCU, now currently with the Receiver. And as I have already held that Clause 3.1 of the Security Sharing Agreement was not void, applying the said condition precedent, the Bank is not entitled to share in the proceeds of Receivership, for as long as the secured liabilities to DFCU have not been met. As between DFCU and the Bank, the

Receiver is directed to proceed accordingly. DFCU and the Bank shall bear each party's own costs in these proceedings.

Dated at Kampala this 15th June 2005

FMS Egonda-Ntende
Judge