

**THE REPUBLIC OF UGANDA,  
IN THE HIGH COURT OF UGANDA AT KAMPALA  
(COMMERCIAL DIVISION)  
CIVIL SUIT NO 239 OF 2013**

**NATIONAL HOUSING & CONSTRUCTION CO LTD} .....PLAINTIFF**

**VERSUS**

**LION ASSURANCE COMPANY LTD} .....DEFENDANT**

**BEFORE HON. MR. JUSTICE CHRISTOPHER MADRAMA IZAMA**

**JUDGMENT**

The Plaintiff originally filed this action by way of summary procedure under Order 36 of the Civil Procedure Rules and leave to defend the action was granted by the court on 13 September 2013 giving leave to the defendant to file a written statement of defence. By the amended plaint filed subsequent to the specially endorsed plaint, the plaintiff's suit against the defendant is for payment of a sum of US\$3,627,762, general damages, and interest on the liquidated demand from the date of demand till payment in full, interest on general damages from the date of judgement till payment in full and costs of the suit.

The facts in support of the cause of action of the plaintiff averred in the plaint is that on 15 July 2011 the plaintiff entered into a contract with Messieurs NH – MKP Builders Ltd to construct 312 blocks each with four floors, with the specified measurements agreed to in Naalya, a suburb in Kampala district at the contract price of the US\$18,138,812. Pursuant to clause 5 of the contract Messieurs MKP Builders SDN BHD was nominated as a subcontractor. Under the contract between the plaintiff and NH – MKP Builders Ltd, the plaintiff undertook to pay 20% of the contract price to the subcontractor as advance payment against receipt of one Advance Payment Guarantee (APG) under the contract and Messieurs NH – MKP was permitted to subcontract some of the work to a nominated subcontractor that is Messieurs MKP SDN BHD Ltd. It was agreed between the plaintiff and NH – MKP Ltd that Messieurs MKP SDN BHD Ltd should take out in favour of the plaintiff an advance payment guarantee before receipt of the advance payment by the plaintiff. On 22<sup>nd</sup> July, 2011 Messieurs NH – MKP builders Ltd entered into a subcontract with MKP builders SDN BHD Ltd to construct the said condominium apartments. Pursuant to clause 3 of the subcontract MKP builders SDN BHD Ltd agreed to provide the plaintiff with an advance payment guarantee from Messieurs Leads Insurance Ltd against receipt of the advance payment. On 29<sup>th</sup> July, 2011 the plaintiff duly transferred to MKP builders SDN BHD Ltd the agreed amounts. The advance payment guarantee issued by Leads

Insurance Company was to expire on 22 December 2012 before the plaintiff received full repayment of the advance payment made to MKP SDN BHD Ltd. MKP SDN BHD was later requested by e-mail dated second of November 2012 to renew their APG. On 16 November 2012 in response to the plaintiff's request, and to avoid termination of the subcontract, Messieurs MKP builders SDN BHD Ltd took out another APG from the defendant.

Under the said APG the defendant agreed with the plaintiff to unconditionally and irrevocably guarantee as primary obligator and not merely surety to pay on first demand and without any objection whatsoever a sum of US\$3,627,762 to the plaintiff on demand. The plaintiff asserts that the guarantee was valid and in full effect from the date of the advance payment guarantee and the head contract and to the plaintiff received for repayment of the monies advanced to Messieurs MKP Builders SDN BHD Ltd but in any event not later than 26 December 2013. The guarantee was executed by the defendant in consideration of the plaintiff terminating or suing on the initial advance payment guarantee issued by Leads Insurance Company Limited. On 4<sup>th</sup> February, 2013 the plaintiff recalled the guarantee demand payment of the sums in the APG from the defendant. On 11 February 2013 the defendant responded to the plaintiff's demand effectively denying liability and advising the plaintiff to have recourse against MKP Builders SDN BHD Ltd. The plaintiff's contention is that the defendant is obliged under the APG issued to unconditionally pay the sums under the guarantee on demand.

The defendant denied liability and in the defence admits that in November 2012 it was approached by officials of MKP builders SDN BHD with a request to provide the guarantee/bond for the sum of US\$ 3,627,760 for the period 27<sup>th</sup> of December, 2012 to 26<sup>th</sup> December, 2013. The defendant asserted that it was the representation of MKP builders SDN BHD that it acquired the guarantee as the requisite for the release of an advance payment by the plaintiff. The defendant accordingly issued the APG referred to on 16 November 2012. The defendant and as to the APG too late to an amount of US\$3,627,760 to be advanced that the plaintiff and was to cover a sum not exceeding the amount to be advanced by the plaintiff and could only become validate or effective from the date of the advance payment under the contract. The defendant further contended in the defence that an APG is by its nature a guarantee issued in respect of money to be advanced after the date of the guarantee. They contend that no advance payment was made by the plaintiff to any person under the APG or after its issuance. The APG was not issued as claimed in consideration of the plaintiff not terminating the contract or suing under the advance payment guarantee issued by Leads Insurance Ltd.

In the alternative and without prejudice the defendant averred that the plaintiff frustrated the contract by refusing to pay against the APG it had issued and therefore suffered no loss. In the further alternative and without prejudice the defendant maintained that the contract to by the plaintiff for the construction of 312 units is tainted with fraud or the claim brought on the basis of the contract and any documents issued under it including the APG is itself a fraudulent claim. The defendant gave the particulars of fraud but there is no need to go into that at the moment.

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The pleadings disclose a narrow controversy as to whether the plaintiff advanced any money against the APG issued by the defendant. Secondly whether the defendant is liable if no money is advanced under the APG in the circumstances of the case. Additionally the plaintiff's counsel and the defendant's counsel in accordance with Order 12 rule 1 of the Civil Procedure Rules gave a summary of the points of agreement in terms of the facts disclosed by the plaintiff and the written statement of defence. The agreed facts are as follows:

1. On 15 July 2011, the plaintiff entered into a contract with NH - MKP builders Ltd to construct 312 condominium apartments split into 12 blocks each with four floors, with each unit measuring approximately 125 meters squared split between two floors in Naalya, a suburb in Kampala district at the contract price of US\$18,138,812 (the main contract).
2. Pursuant to clause 2 of the main contract the plaintiff undertook to pay NH – MKP builders Ltd 20% of the contract sum as advance payment against receipt of an advance payment guarantee from a bank or insurance company that was acceptable to the plaintiff and in an amount and currency equivalent to the advance payment.
3. On 22 July 2011 NH – MKP builders Ltd entered into a subcontract with MKP builders SDN BHD Ltd to construct the said condominium apartments at a contract price of US\$17,959,220 (the subcontract).
4. Pursuant to clause 2 of the subcontract, NH – MKP builders Ltd undertook to pay MKP builders SDN BHD Ltd 20% of the contract sum in advance against receipt of an advance payment guarantee from a bank or insurance company acceptable to NH – MKP builders Ltd and in the amount and currency equal to the advance payment.
5. By Bond No. NIL/01 – B52/001434/2011 dated 27<sup>th</sup> of July, 2011 leads insurance company limited issued an advance payment guarantee in an amount not exceeding US\$3,627,762.
6. By endorsement No. LIL/-01/B52/01434/2011, leads insurance company limited altered the date of expiry of bond number LIL/01-B52/001434/2011 to 27<sup>th</sup> December 2012.
7. By Bond No. B1/BON/POL/0007481 dated 16<sup>th</sup> of November 2012 the defendant, upon application by MKP builders BHD SDN Ltd, issued an advance payment guarantee undertaking to pay to the plaintiff a sum not exceeding US\$3,627,762.
8. It was further agreed that the terms of the guarantee included the following:

- a. The Defendant would unconditionally and irrevocably guarantee as primary obligator and not mere surety to pay on first demand and without any objection whatsoever a sum not exceeding US\$3,627,762.
- b. The guarantee was to remain valid and in full effect from the date of the advance payment under the contract until the plaintiff receives full payment of the same amount from the contractor but in any case not later than 26 December 2013.

The agreed issues for trial are:

- a) Whether there was any advance payment made under the guarantee dated 16th of November 2012?
- b) Whether the defendant is liable to pay the plaintiff any money and that the advance payment guarantee dated 16th of November 2012?
- c) If issue (b) is answered in the affirmative, what amounts payable?
- d) What remedies are available to the parties?

At the hearing of the suit the plaintiff was represented by Counsel Isaac Walukaga of MMAKS advocates while the defendant was represented by counsels Earnest Kalibala appearing jointly with Counsel Frederick Mpanga from AF Mpanga and company advocates.

The plaintiff called Emma Wangota, the Legal Manager of the plaintiff who testified as PW1 while the defendants called two witnesses Mr Godfrey Buyondo as DW1 and Mr Newton Jazire MD of the defendant as DW2 and closing arguments by counsel were made in written submissions.

**1. Whether there was any advance payment made under the guarantee dated 16<sup>th</sup> of November 2012?**

**Submissions on Issue 1 by Plaintiff's Counsel**

The plaintiff's counsel relied on section 101 of the Evidence Act Cap 6 Laws of Uganda on the burden of proving facts relevant to an issue as being on the party asserting those facts. He submitted that the guarantee dated 16<sup>th</sup> of November 2012 is the Advance Payment Guarantee Exhibit P10 (APG). The defendant's contention is that it is not liable to pay the sum set out in the APG because no advance payment was made by the plaintiff after execution of the APG. He submitted that this contention stems from paragraph 5 (e) of the WSD, paragraphs 14 and 15 of

the written testimony of the Godfrey Buyondo DW1 and paragraph 13 of the witness statement of Newton Jazire DW2. On the other hand Emma Wangota PW1 testified that the defendant executed an APG in favour of the plaintiff on 16<sup>th</sup> November, 2012 and in paragraph 19 thereof and cross examination he testified that the APG was premised on the advance payment under the subcontract exhibit P2 between NH - MKP and MKP Builders SDN BHD Ltd. The first paragraph of exhibit P10 provided that:

"In accordance with the provision of the contract referenced above, in relation to advance payments of the above-mentioned contract, MKP builders SDN BHD Ltd... shall deposit with the employer an insurance guarantee..."

Clause 2 of the sub contract exhibit P2 provided that the contractor hereby undertakes to pay the subcontractor 20% of the contract sum in advance against receipt of an advance payment guarantee from a bank. The testimony of PW1 is that on 18<sup>th</sup> July, 2011, the plaintiff received a letter exhibit P 15 from NH - MKP Builders Ltd requesting the plaintiff to pay MKP Builders SDN BHD Ltd a sum of US\$3,591,824 being 20% of the subcontract price. The subcontract price was set out in exhibit P2 and amounts to US\$17, 959,220. The relevant part of the letter requested payment of MKP Builders SDN BHD the equivalent of US\$3,591,844 in Ugandan currency. MKP Builders SDN BHD authorised payment according to the letter. Prior to the request, MKP Builders SDN BHD Ltd wrote to the plaintiff on 18<sup>th</sup> July 2011 in exhibit D16 requesting that the advance payment is remitted to MKP Builders SDN BHD (Uganda) Ltd. They wrote authorising National Housing and Construction Company to release advance payment of worth US\$3,591,844 to the account of MKP Builders SDN BHD (Uganda) Ltd. The payment was wired by the plaintiff to MKP Builders SDN BHD (Uganda) Ltd account and is evidenced by exhibits P6, P14, D2 and P15. The contention of the defendant was that no payment was made after the issuance of the APG exhibit P10. DW2 testified that neither the bond proposal form nor exhibit P10 provide an advance payment after execution of the APG. He further stated that the defendant was as a matter of insurance conventions and practice under the impression that the plaintiff would make an advance payment in favour of MKP Builders SDN BHD Ltd. The plaintiff's counsel submitted that this is not supported by any documentation. On the contrary, exhibit P10 indicates that the advance payment was in accordance with the subcontract exhibit P2. When cross-examined about the subcontract exhibit P2 DW1 testified that he did not look at it. He added that an advance payment was money paid to the contractor to mobilise resources and start work. The defendant had not bothered to ascertain if MKP Builders SDN BHD Ltd had started the works at the time the APG was issued. He was aware of one earlier advance payment made by the plaintiff to MKP Builders SDN BHD. He testified in paragraph 16 that it was dishonest for the plaintiff to claim that the APG covered a disbursement which had been made in July 2011. The plaintiff's counsel submitted that the net effect of the testimony of PW1 taken together with the first paragraph of the APG exhibit P2, P 14, P 16 and D2 is that an advance payment had been made under the subcontract prior to the execution of the

APG. The defendant's contention on the other hand is that the advance payment was supposed to have been made after execution of the APG and is not in tandem with the APG on the following grounds:

Firstly, the APG exhibit P10 signed by the defendant packaged with a deliberate choice of words as confirmed in DW2's testimony indicates that it was made in accordance with the provisions of the contract referenced above in relation to advance payment of the above contract;

Secondly, the only operative term on the APG on the advance payment was the first paragraph of the APG. The advance payment was in accordance with the subcontract exhibit P2 between MKP Builders and SDN BHD Ltd.

Thirdly, the subcontract provides in clause 2 that NH - MKP builders undertook to pay MKP builders SDN BHD 20% of the contract sum upon receipt of an advance payment guarantee.

Fourthly, the 20% of the contract price was indeed paid by NH - MKP Builders SDN BHD.

Counsel submitted that DW1 and DW2 confirmed that the APG was prepared by the defendant. The defendant indicated in the APG that the advance payment was made in accordance with the subcontract. This is binding on the defendant and who cannot choose to walk away from this term when it does not suit its interests. He contended that the defendant was fully aware of the terms it was binding and the APG is construed strictly as it appears. He relied on the holding in **Access Financial Services PLC Ltd vs. Khayongo Patricia Rutiba HCCS No 61 of 2007**. In that case the parties to the suit entered into what appeared to be a loan agreement. Among the issues for trial was the scope of the agreement. It was held by Kiryabwire J (Judge of the High Court as he then was) that the defendant knew and was aware of what she was signing at the time she signed the loan agreement. She knew and was aware of the terms and conditions she was binding herself to.

The plaintiff's counsel further submitted that the defendant is barred by estoppels from denying that the advance payment under the APG was that made in accordance with the subcontract. The doctrine of estoppels was discussed in the case of **Pan African Insurance Company (U) Ltd versus International Transport Association HCCS 667 of 2003**. In that case the plaintiff made a payment to the defendant on the basis of a guarantee in favour of the defendant by a third party. One of the issues in contention was whether the plaintiff having represented to the defendant that it was entitled to a payment and even made part payment was barred by estoppels from claiming a refund of monies paid to the defendant after the failure of the third-party to make good on its obligations to the plaintiff. Honourable Justice Lameck Mukasa held that:

“...the doctrine of estoppels by conduct prevents the party against whom it is set up from denying the truth of the matter. The principle is that where a party has by his declaration,

act or omission intentionally caused the other to believe a thing to be true and act upon such belief, he cannot be allowed to deny the truthfulness of that thing”.

The defendant in this case made a declaration to the plaintiff that the advance payment in respect of the APG was that in the subcontract. It caused the plaintiff to believe this to be true and act upon that belief. The defendant should therefore not be allowed to deny the truthfulness of the declaration as contained in paragraph 1 of the APG. Furthermore the plaintiff's counsel invited the court to answer Issue No 1 in the affirmative as the advance payment made under the APG exhibit P10 was that made in accordance with the subcontract exhibit P2.

### **Submissions in Reply on Issue 1 by Defendant's Counsel**

In reply the defendants counsel also set out the factual background that I do not need to repeat here. The submissions of the defendants counsel are as follows:

The making of an advance payment is a question of fact. The Lion Advance Payment Guarantee is dated 16<sup>th</sup> of November 2012. The answer to whether any advance payment was made against the guarantee dated 16<sup>th</sup> of November 2012 does not lie in documents preceding its existence or in an attempt to twist the construction of the wording in the Lion APG. He contended that the document in issue is an advance payment guarantee and not an 'advanced payment guarantee'. Taking into consideration the nomenclature and well settled position that this type of instrument is used with reference to payment to be made after it has been completed; its existence can only be a condition precedent to the payment to which it relates. An advance payment guarantee cannot be issued to cover an existing liability or an advance made months prior to its own existence. As such, payments made prior to its existence cannot properly be said to be made under it. The payments would constitute past consideration under the contract of guarantee or in this case under the Lion APG. The defendant's counsel submitted that there is no dispute as to the fact that the sums shown to have been paid out by the plaintiff were made or advanced in July and October 2011. Such advances or payments could not have been made in contemplation that the Lion APG (which was to be granted more than 16 months later) would guarantee the sums so advanced. It could not have been contemplated that the Lion APG would be created in the course of what the plaintiff referred to in exhibit P12 as "failure by MKP builders SDN BHD to implement the contract" and then be used to cover an advance payment or payment already made.

The defendant's counsels submitted that the correct answer to issue number 1 is unequivocal in that no advance payment was made under the guarantee dated 16<sup>th</sup> of November 2012. The submission is based on the failure by the plaintiff to provide any evidence to prove such advance payment. Counsel for the plaintiff concentrated on attacking the evidence of DW1 and DW2 rather than on providing evidence of payments by the plaintiff to MKP Builders SDN BHD Ltd made after 16<sup>th</sup> of November 2012. The erroneous interpretation of a paragraph of the Lion APG

provides no assistance as the Lion APG did not relate back to the payment made 16 months prior to its existence.

The defendants counsel pointed out that while PW1 provided the exhibits in court, he admitted that he joined the plaintiff in June 2011. By the time he was employed, the arrangements with MKP Builders SDN BHD were already in place. He was not part of the Contracts Committee of the plaintiff and did not draft the main or subcontract. He had little to do with the matter at hand. A scrutiny of the documents revealed that PW1 originated only exhibit D15 on 15<sup>th</sup> March, 2013. It follows that a significant part of his evidence were based on conjecture, assumptions and illusions rather than actual knowledge.

The main contract which was executed on 15<sup>th</sup> July, 2011 provided in clause 2 thereof that an advance equivalent to 20% of the contract sum would be made against receipt of an advance payment guarantee from a bank or insurance company that is acceptable to the plaintiff. A similarly worded clause is found in the subcontract executed on 22<sup>nd</sup> July, 2011. On the basis of the contract sum in the main contract, such an advance payment was then equivalent to US\$3,627,762.40. From the wording it was envisaged and understood that the availability of the advance payment guarantee issued by a bank or insurance company acceptable to the plaintiff would be the basis for or of an advance payment of an amount equal to 20% of the contract sum. Consequently it was always understood that the advance payment would come after receipt of an Advance Payment Guarantee by the plaintiff. This is the form of arrangement PW1 confirmed during cross examination when he said that the contents of clause 2 of exhibit P1 are correct and were acceptable to the plaintiff. The first guarantee was in such acceptable form and the form was the same for the second guarantee.

On 27<sup>th</sup> July, 2011, Leads Insurance Ltd issued the Leads APG for a sum of US\$3,627,762 and it was exhibited as exhibit P3. The guarantee was extended by way of endorsement from 27<sup>th</sup> July, 2012 to 27<sup>th</sup> of December, 2012. The endorsement is marked exhibit D10. The date on which the two advance payments were made are shown in exhibit P5 and P6 and lead to the conclusion that there was no advance payment made under the Lion APG.

The defendants counsel further pointed out that though exhibit P14 was processed for payment on 14<sup>th</sup> of July 2011, which is before the execution of the main contract, it was paid on 28<sup>th</sup> July 2011, a day after the issuance of the Leads APG on 27<sup>th</sup> July 2011. From the evidence payments were made subsequent to the receipt by the plaintiff of one advance payment guarantee in the form acceptable to it. This was the Leads APG court exhibit P 15 which also mentioned as an advance payment guarantee from HI Fund International Bank. It follows that the arrangement where advance payment is made after receipt of an APG also applies to the Lion APG. The Lion APG was to predate payment and it was not intended to and did not secure obligations which were already in place before its existence. For this proposition, the defendant's counsel relied on the testimony of DW1 and DW2 who re-affirmed the practice of issuing the APG before advance



payment is made to the Contractor by the Employer. Lastly the defendants counsel relies on the cross-examination of PW1 on 10<sup>th</sup> of September 2015 where he testified that Certificate No 1 was paid under the APG issued by Leads Insurance and no money was paid to anybody under the APG issued by Lion Insurance. For emphasis the dates of exhibit P5 and P14 together with exhibit P6 and they show that payments were made prior to the issuance of the Lion APG. It is therefore strange for the plaintiff's counsel to submit that the defendant made a declaration to the plaintiff who believed the same to be true and that the plaintiff acted on that belief. The plaintiff did not advance any money on the strength of the advance payment guarantee. It is therefore a preposterous submission which should be rejected. Counsel emphasised that there is no doubt that advance payments were made prior to the Lion APG even being contemplated. There could be some confusion as to whether payment was made as a result of the Leads APG. He prayed that exhibit P 15 should be examined very carefully because the heading thereof provides clearly that it refers to an advance payment for the contract. It demonstrates that the process of the advance payment was ongoing prior to the Leads APG itself being issued and prior to execution of the main contract on 15<sup>th</sup> July, 2011. It also makes reference to Certificate No. 1 initiated on 14<sup>th</sup> July, 2011 before the execution of the main contract and requests for advance payment for the Naalya Pride Project to be made to MKP Builders SDN BHD (Uganda) Ltd. The Leads APG is dated 27<sup>th</sup> of July 2011 and is not even referred to in what is being called the instructions by NH - MKP Builders Ltd to make any advance payment available.

In conclusion issue number 1 should be answered in the negative because no money was advanced under the Lion APG. This proposition is supported by the unequivocal testimony of PW1 who is an official of the plaintiff.

I have further considered other submissions and the above submission deals with the first issue and I do not need to refer to further submissions on the issue for the moment.

### **Submissions in Rejoinder on Issue No. 1**

In rejoinder on the first issue counsel for the plaintiff submitted that the defendant's case are based on the contention that no advance payment was made under the advance payment guarantee exhibit P10.

Counsel submitted that the answer to issue number one can only be extracted from clause 1 of the APG exhibit P10 which provides that in accordance with the provision of the contract referenced above, in relation to advance payments of the above-mentioned contract, MKP Builders SDN BHD Ltd shall deposit with the employer an insurance guarantee. The clause essentially has the following import:

The APG referred to the contract for construction of condominium units between the plaintiff and NH – MKP and consequentially the subcontract between NH - MKP and MKP Builders SDN BHD. Secondly, the advance payment referred to in the APG was in the contract mentioned

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above. Thirdly, the above head contract only had one advance payment to be made by the plaintiff. The beneficiary of the advance payment was MKP Builders SDN BHD as a nominated subcontractor. Fourthly, no mention was made of any payment to be made after execution of the APG which is why it is couched with reference to advance payments that were made in the contract that the defendant knew at the time of execution of the APG had been made.

The defendant's argument is that no advance payment was made is out of context with the wording of the advance payment guarantee instrument. This instrument clearly provides that it had been executed in accordance with the advance payment provided in the main contract. Pursuant to the terms of the APG, it was to be obtained by MKP Builders SDN BHD in favour of the plaintiff. The advance payment to the benefit of MKP Builders SDN BHD was provided for in the sub contract exhibit P2. In a letter dated 18<sup>th</sup> of July, 2011 exhibit P15, NH - MKP Builders Ltd instructed the plaintiff to pay 20% of the contract price to the MKP Builders SDN BHD. Through another letter dated 18<sup>th</sup> of July 2011 exhibit P 16, MKP Builders SDN BHD instructed the plaintiff to make the advance payment in favour of MKP Builders SDN BHD (U) Ltd. MKP Builders SDN BHD Ltd has never complained that no advance payment was made to it as provided for in the sub contract exhibit P2. It is not in dispute that the defendant did not at any one time complain to the plaintiff prior to making a call on the APG that no advance payment had been made as required by the contract. This complaint only came in after a call on the APG had been made by the plaintiff.

The plaintiff's counsel submitted that it is important to appreciate the intention of the parties at the time the APG was executed. The question was whether the wording of the APG expresses an intention of the parties that the plaintiff shall make an advance payment after the execution of the APG? Secondly, did the parties, MKP Builders SDN BHD and the defendant intended to rely on advance payments made under the main contract and subcontract? Thirdly it is untenable that the defendant construed the APG to mean that MKP Builders SDN BHD was still entitled to yet another advance payment out of the one in the subcontract? Fourthly, was the intention of the parties that payment made after the advance payment in the head contract and subcontract would also be done as "advance payments"? Lastly, were such payments made after payments in the head contract and subcontract referred to in the APG the advance payment intended in the APG?

Counsel defined and advance payments to mean a payment made before it is due. According to **Black's Law Dictionary**, an advance payment is a payment in anticipation of a contingent or fixed future liability or obligation. The defendant's testimonies of DW1 and DW2 at that at the time the APG was executed is that the contract was already underway and the plaintiff had obtained previous guarantees from Leads Insurance Company which the defendant was aware of. This meant that only one advance payment referred to the APG were those made under this head contract and subcontract exhibit P2.

Counsel submitted that the plaintiff did not make any undertaking to make any further advance payment under the APG. Secondly, the intention of MKP Builders SDN BHD and the defendant was to make reference to advance payment under the subcontract and head contract. Thirdly, it is not tenable that the defendant believed that another advance payment would be made to MKP Builders SDN BHD outside that mentioned in the contracts and that any such payments would also be termed advance payments.

In the premises the plaintiff's counsel reiterated submissions that the advance payment in the APG was that with reference to the subcontract and this had been made in favour of MKP Builders SDN BHD.

With regard to the doctrine of estoppels, the plaintiff's counsel submitted that his submission had been misunderstood. The point was that the defendant made a representation to the plaintiff through the APG that it had issued in favour of the plaintiff that the APG had been executed with reference to the advance payments on the contracts. It was against this representation that the plaintiff continued its relationship with MKP Builders SDN BHD. Having acted on the defendant's representation, the defendant should not be seen to shift the position that it understood that the advance payments made under the APG meant future payments. That is the mischief estoppels would guard against and it was being used as a shield and not a sword.

### **Judgment on Issue No. 1**

I have carefully considered the plaintiffs submissions as well as the defendant's submissions and the authorities referred to. I have also considered the exhibits; the subject matter of the submissions namely exhibits P 10 which is the Advance Payment Guarantee (APG) and exhibit P2 which is the contract or subcontract. The primary premise on which the plaintiff relies is the wording of clause 1 of exhibit P10. Paragraph 1 provides as follows:

"In accordance with the provisions of the Contract referenced above, in the relation to Advance Payments of the above-mentioned contract, MKP Builders SDN BHD Ltd of P.O. Box 9421, Kampala (hereinafter called "contractor") shall deposit with the Employer an Insurance Guarantee to guarantee its proper and faithful performance of the obligations imposed by the said clause of the contract, in the amount of US\$3,627,762 (United States dollars three million six hundred twenty-seven thousand seven hundred sixty-two.)..."

In the "contract referenced above" it is written that it is for the "CONSTRUCTION OF 312 CONDOMINIUM APARTMENTS SPLIT INTO 12 BLOCKS EACH FOUR FLOOR EACH UNIT IS APPROXIMATELY 135 M<sup>2</sup> SPLIT BETWEEN TWO FLOORS INCLUSIVE OF OVERHEADS".

The key phrase in the above quoted clause 1 is: "in relation to Advance Payments of the above-mentioned contract". The Plaintiff's Counsel submitted on the same premises.

What are the advance payments of the above mentioned contract? The provision refers to "advance payments" in the plural rather than "advance payment" in the singular. We can start with the specific provision of the first main contract which is between the Plaintiff and NH – MKP Builders Ltd. This was tendered in evidence as exhibit P1 and is dated 15<sup>th</sup> July 2011. Clause 2 thereof provides as follows:

"The Employer hereby undertakes to pay the Contractor 20% of the contract sum as advance payment against receipt of an advance payment guarantee from a Bank or Insurance Company that is acceptable to the Employer, and in the amount and currency equal to the advance payment."

Secondly, clause 3 provides that:

"The Contractor hereby undertakes to provide the Employer with a performance security equivalent to 10% of the agreed contract sum in the currency in which the contract sum is payable."

There is no controversy about clause 1 which stipulates that the contract sum is US\$ 18,138,812 inclusive of VAT. Secondly, the main contract was subcontracted to a subcontractor and the subcontract was admitted in evidence as exhibit P2 and is between NH – MKP Builders Ltd (the Contractor under the main contract and MKP Builders SDN BHD of Malaysia, the subcontractor). In clause 1 of exhibit P2 the contract provides that the subcontractor would provide the services of construction under the main contract for a consideration of US\$ 17,959,220. Clause 2 reproduces clause 2 of the main contract exhibit P1 and provides as follows:

"The Contractor hereby undertakes to pay the Sub Contractor 20% of the contract sum in advance payment against receipt of an advance payment guarantee from a Bank or Insurance Company that is acceptable to the Contractor, and in the amount and currency equal to the advance payment."

Clause 3 of exhibit P2 provides that the Advance Payment Guarantee shall be in favour of National Housing & Construction Company Ltd (The Plaintiff). Finally clause 4 provides that:

"The Sub Contractor hereby undertakes to provide the Contractor with a performance security equivalent to 10% of the agreed contract sum in the currency in which the contract sum is payable."

The controversy for resolution is whether the advance payments were future payments to be made under that contract or payments which were made pursuant to that contract where that they

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had already been paid or made. The defendant's defence for avoiding liability rests on the proposition that the advance payment guarantee only guaranteed a future event of the beneficiary who is the plaintiff making an advance payment to MKP Builders SDN BHD Ltd possibly through the main contractor NH – MKP Builders Ltd. The Defendant's contention is that so long as no advance payment is made, the security of the APG provided could not be enforced against the defendant.

It is also a matter of fact and an agreed fact that after the issuance of the advance payment guarantee exhibit P10 on 16<sup>th</sup> November 2012, no further payment in terms of an advance was made to the Contractor by the Employer or its agent. The suit on issue number 1 will mainly depend on interpretation rather than any controversy of fact. There are some facts which need to come out pursuant to a consideration of exhibits P1 and P2 which are admitted documents. This is the fact that exhibit P1 is between the plaintiff and NH – MKP Builders Ltd and is dated 15<sup>th</sup> of July 2011. Secondly, exhibit P2 which concerns the APG under consideration is a subcontract between NH - MKP Builders Ltd and MKP Builders SDN BHD. The subcontractor is MKP Builders SDN BHD of Malaysia. The plaintiff is not privy to this subcontract neither is the defendant privy to the subcontract. However, the subcontract clearly stipulates that the Advance Payment Guarantee shall be in favour of National Housing & Construction Company Ltd, which is the plaintiff. Specifically clause 2 of the contract provides that the Contractor which is defined as NH - MKP Builders Ltd undertakes to pay the subcontractor 20% of the contract sum in advance against receipt of an Advance Payment Guarantee from a bank or insurance company that is acceptable to the contractor and in the amount and currency equal to the advance payment. It follows that the advance payment was going to be made to the subcontractor which is MKP Builders SDN BHD by NH – MKP Builders Ltd. National Housing and Construction Company Ltd is not a party to the subcontract. It is only a beneficiary to the Advance Payment Guarantee. The plaintiff was under no obligation under this arrangement to make any advance payment to the subcontractor. The plaintiff could only have fulfilled its obligation under the contract exhibit P1 between it and NH – MKP Builders Ltd.

The question here is therefore whether the payment as a matter of fact had been made and the answer seems to be that agreed by the parties that NH – MKP Builders Ltd after the issuance of the Advance Payment Guarantee exhibit P10 did not make any advance payment at all. On the other hand the Plaintiff had earlier paid the Contractor or subcontractor before the APG in question was issued on 16<sup>th</sup> November 2012. The plaintiff's submission therefore depends on the wording of the APG issued by the defendant in terms of the APG under the contract.

A simple conclusion based on a plain and literal reading of clause 2 of exhibit P2 would lead to the conclusion that the advance payment secured by the guarantee could be only against receipt of an Advance Payment Guarantee from a bank or insurance company. In other words the Advance Payment Guarantee envisaged under clause 2 is one which would be used to secure advance payment from the Contractor Messieurs NH - MKP Builders Ltd who was expected to

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advance the sum to MKP Builders SDN BHD of Malaysia. This seems at first glance to overcome the argument that the advance payment was already made and therefore what the APG secured was an obligation that arose earlier under the contract however the Plaintiff relies on uncontested evidence that payment had been made prior to issuance by the Defendant of the new APG of 16<sup>th</sup> November 2012.

As I have noted above the plaintiff is not privy to the contract exhibit P2 neither is the defendant a party. The plaintiff is a beneficiary mentioned in exhibit P2 under clause 3 thereof which contract is between NH – MKP Builders Ltd and MKP Builders SDN BHD of Malaysia. I therefore consider the principles of law concerning demands made on an Advance Payment Guarantee upon the occurrence of the risk insured against and for which security of the APG is issued as well as more evidence of what happened before coming to a conclusion on the issue.

In a ruling delivered on the 16<sup>th</sup> of September 2013 and in an application for leave to defend the action I did consider some of the judicial precedents. This was in **Miscellaneous Application No. 411 of 2013** where the defendant was granted leave to defend the claim for US\$ 3,627,762 undertaken in the APG in question to be paid to the Plaintiff under the terms thereof. I also subsequently considered these principles in **Lamba Enterprises Ltd vs. Attorney General HCMA No.286 of 2013 arising from High Court Civil Suit No. 245 of 2013** decided on the 14<sup>th</sup> of October 2013. According to Geraldine Mary Andrews in the **Law of Guarantees Second Edition 1995** at page 443:

"Performance Bonds are essentially unconditional undertakings to pay a specified amount of money to a named beneficiary, usually on demand, and sometimes on the presentation of certain specified documents."

It is an undertaking to pay a specified sum to the beneficiary in the event of breach of contract. Where the beneficiary seeks payment in accordance with the terms of the bond, the bank or insurance company must pay. According to Geraldine Mary Andrews (supra) at page 444:

"It is well established that if the beneficiary seeks payment in accordance with the terms of the bond, the bank must pay, regardless of how unfair that might be to the account party. This is exemplified by the leading case of Edward Owen Engineering Ltd versus Barclays Bank International Ltd [1978] QB 159."

A demand made according to the terms of the performance bond must be paid. The learned authors in the Law of Guarantees (supra) also postulate at page 460 that:

"It is highly unlikely that the account party would ever succeed in persuading an English court to grant him an injunction restraining the bank which issued the Performance Bond (or, if there is a chain, the bank which is liable to pay under it) from making payment, once a demand has been made against it in accordance with its terms."

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There are exceptions to the general rule on the duty or obligation of the bank or insurance company to pay. What are these general exceptions? The leading general rule is the case of **Edward Owen Engineering Ltd v Barclays Bank International Ltd [1978] 1 All ER 976** which was about a performance guarantee. The Libyan customers, before any contract was concluded, stipulated that there should be a performance guarantee. It was to be a condition precedent to their entering into any contract at all. On the other hand the obligation of the bank or insurance company is to pay without enquiring about what is going on between the buyer and seller. Lord Denning held that any dispute between the buyer and seller must be settled between themselves. The bank or insurance company has to pay except in cases of fraud. He quoted the American Practice in the case of **Sztejn v J Henry Schroder Banking Corp ((1941) 31 NY Supp 2d 631 at 633)** that:

‘It is well established that a letter of credit is independent of the primary contract of sale between the buyer and the seller. The issuing bank agrees to pay upon presentation of documents, not goods. This rule is necessary to preserve the efficiency of the letter of credit as an instrument for the financing of trade. ... the principle of the independence of the bank’s obligation under the letter of credit should not be extended to protect the unscrupulous seller.’

In **Edward Owen Engineering Ltd v Barclays Bank International Ltd** (supra) the facts clearly show that the performance bond was a condition precedent to entering into a contract at all. In the ruling for leave to defend the summary suit I cited the said authorities for the same principles. I will repeat the judicial authorities in this judgment. Because the issuance of the performance guarantee was a condition precedent to the execution of the contract and carrying out of obligations there under the facts of the **Edward Owen Engineering Ltd v Barclays Bank International Ltd** case (supra) are distinguishable from the facts and circumstances of this case where the Advance Payment Guarantee was issued after the advance payment had been made by the intended beneficiary who is the plaintiff. Similarly in the case of **Gold Coast Ltd versus Caja de Ahorros del Mediterraneo and others [2002] 1 All ER 142**, the buyers obligation to make each stage payments was conditional upon the simultaneous delivery of a prescribed refund guarantee from the defendant banks to the buyers bank in the amount of the payment. The guarantee was issued prior to payments and was a condition precedent. The same principle appears on the analogy of the same principles applicable to letters of credit as held in the case of **United City Merchants (Investments) Ltd and others v Royal Bank of Canada and others [1982] 2 All ER 720** a judgment of the House of Lords. Lord Diplock who considered the purpose of the law on letters of credit held at page 725 that:

“The whole commercial purpose for which the system of confirmed irrevocable documentary credits has been developed in international trade is to give to the seller an assured right to be paid before he parts with control of the goods and that does not permit

of any dispute with the buyer as to the performance of the contract of sale being used as a ground for non-payment or reduction or deferment of payment.

To this general statement of principle as to the contractual obligations of the confirming bank to the seller, there is one established exception: that is, where the seller, for the purpose of drawing on the credit, fraudulently presents to the confirming bank documents that contain, expressly or by implication, material representations of fact that to his knowledge are untrue.”

The first rationale gives the nature of the performance bond or confirmed irrevocable documentary letters of credit as being a security given prior to parting with the control of the goods. In other words the person parting with something valuable is assured of being paid for it or compensated before he parts with possession of the thing for which security is warranted. The exceptions to the rule are that the seller will not falsify documents that it is fulfilling or has fulfilled its obligations and present the falsehood to the bank or insurance company which issued the performance bond. In cases of letters of credit the seller is assured by a guarantee before parting with possession of his or her goods. In the cases reviewed the performance bond is a condition precedent to the supply of goods.

Applying the same rationale for the issuance of an APG to the facts and circumstances of this case the Contractor NH – MKP Builders Ltd was supposed to be assured before it paid MKP Builders SDN BHD of Malaysia the 20% obligation under clause 2 of exhibit P2 which I shall repeat here for emphasis and ease of reference because it provides:

"The Contractor hereby undertakes to pay the Subcontractor 20% of the contract sum as advance payment against receipt of an advance payment guarantee from a Bank or Insurance Company that is acceptable to the Contractor, and in the amount and currency equal to the advance payment."

The fact that the 20% mentioned above is the sum claimed by the plaintiff is not in dispute. Secondly the fact that the Plaintiff is the beneficiary mentioned in the contract exhibit P2 is not in dispute and I need not determine any controversy in relation thereto. What is material for now is the interesting fact that neither the Plaintiff nor the defendant are privy to exhibit P2 which is the foundation of the APG exhibit P10 that formed the basis of the Plaintiffs claim in this suit. Exhibit P10 was issued pursuant to the subcontract in exhibit P2 namely on request of MKP Builders SDN BHD Ltd of Malaysia presumably and as will be established who contracted the defendant to issue an APG in favour of the plaintiff. The detailed review of the situation was given in my interlocutory ruling.

The precedents reviewed have one common feature which is that at least one of the parties who requested for the issuance of a performance bond is normally privy to the underlying contract. In this case the contract exhibit P2 shows that the Contractor is NH – MKP Builders Ltd and the  
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Subcontractor is MKP Builders SDN BHD Ltd of Malaysia. The advance payment is to be made by the Contractor namely NH –MKP Builders Ltd to the subcontractor MKP Builders SDN BHD Ltd. MKP Builders SDN BHD was contracted to carry out the main contract under the same terms as in the main contract between the Plaintiff which is the Employer and NH – MKP Builders Ltd who is described as the Contractor and the contract thereof is exhibit P1.

As noted there is no contractual relationship between the Plaintiff and MKP Builders SDN BHD Ltd other than the contractual clause 5 of the main contract exhibit P1 which refers to MKP Builders SDN BHD of Malaysia as the nominated subcontractor. The subcontract as noted above is between NH – MKP Builders and MKP Builders SDN BHD Ltd. They were required to advance NH – MKP Builders Ltd 20% of the contract price of US\$ 18,138,812 under clause 2 of the main contract exhibit P1. NH MKP Builders Ltd subcontracted MKP Builders SDN BHD of Malaysia to do the work and executed exhibit P2 which is a contract between NH – MKP Builders and MKP Builders SDN BHD of Malaysia. Under exhibit P2 which is the subcontract NH – MKP Builders Ltd was required to advance 20% of US\$ 17,219,220 under clause 2 thereof to the subcontractor MKP Builders SDN BHD Ltd the subject matter of the claim in this suit.

The advance payment guarantee (APG) is exhibit P10. It is issued by the defendant in favour of the beneficiary National Housing and Construction Company Ltd who is the Employer defined in exhibit P1 which is the main contract.

Exhibit P10 which is the Advance Payment Guarantee issued by the Defendant is addressed to the beneficiary National Housing and Construction Company Ltd (The Plaintiff) and concerns the construction of 312 condominium apartments split into 12 blocks each with 4 floors in Naalya and provides as follows:

“To: NATIONAL HOUSING AND CONSTRUCTION COMPANY LTD,  
P.O. BOX 569,  
KAMPALA UGANDA.

CONTRACT: CONSTRUCTION OF 312 CONDOMINIUM APARTMENTS SPLIT INTO 12 BLOCKS EACH 4 FLOOR. EACH UNIT IS APPROXIMATELY 132 M2 SPLIT BETWEEN TWO FLOORS INCLUSIVE OF OVERHEADS.

BOND NO. B1/BON/POL/0007481 Date: 16<sup>th</sup> November, 2012.

Dear Sirs,

"In accordance with the provisions of the Contract referenced above, in relation to Advance Payments of the above-mentioned contract, MKP Builders SDN BHD Ltd of

PO Box 9421, Kampala (hereinafter called "Contractor") shall deposit with the Employer an Insurance Guarantee to guarantee proper and faithful performance of the obligations imposed by the said Clause of the Contract, in the amount of US\$3,627,762 (United States Dollars three million, six hundred twenty seven thousand sixty two only.)

We, the undersigned LION ASSURANCE COMPANY LIMITED OF P.O. BOX 7658, KAMPALA legally domiciled in KOLOLO PLOT 50 WINDSOR CRESCENT (hereinafter called the "guarantor") as instructed by the Supplier, agree unconditionally and irrevocably to guarantee as primary **Obligator** and not as Surety merely, the payment to the Employer on its first demand without whatsoever objection on our part and without its first claim to the Supplier, in the amount not exceeding USD 3,627,762.00 (United States Dollars three million, six hundred twenty seven thousand sixty two only.)

We further agree that no change or addition to or other modification of the terms of the contract or of the works to be performed thereunder or of any of the Contract documents which may be between the Employer and the Contractor shall in any way release us from any liability under this guarantee, and we hereby waive notice of any such change addition or modification.

This guarantee shall remain valid and in full force from the date of the advance payment under the contract until the **Employer** receives full repayment of the same amount from the contractor and in any case not later than 26/12/2013.

Signed and sealed by .....  
NEWTON JAZIRE

On behalf of LIOAN ASSURANCE COMPANY LTD

In the capacity of OPERATIONS MANAGER

In the presence of .....  
RITA NAMAKIIKA NANGONGO  
COMPANY SECRETARY"

The first observation is that the clause of the contract referred to in paragraph 1 of the APG is not specified. By analogy because it deals with a specified amount to be paid, it is clause 2 of exhibit P2 earlier on cited. Secondly under clause 1 the Defendant undertook to guarantee proper and faithful implementation of the contract.

I have considered the controversy as revealed in the submissions of counsel and based on the pleadings, the documents exhibited, the testimonies of PW1, DW1 and DW2 which relate to

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enforcement of clause 2 of exhibit P2 and the undertaking in exhibit P10 which is the APG cited above.

The defendant's contention on a matter of fact is that no advance payment had been made after 16<sup>th</sup> of November 2012 when the APG was issued. This is not disputed by the plaintiff. The corollary argument is that Exhibit P10 which is the APG was meant by legal doctrine, interpretation and practice to secure future advance payment to the subcontractor. Lastly that the defendant did not take over an existing obligation where the advance payment had already been made under the contract referred to as argued by the Defendant's counsel.

As far as legal doctrine and interpretation of the wording of the APG is concerned the plaintiff's argument simply is that in clause 1 of exhibit P10, the defendant guaranteed obligations imposed by the referenced contract and this would be any obligation imposed on the Employer that included an advance payment which had already been made under the contract.

This controversy is whether this issue will be resolved on the basis of the first doctrine that a guarantee essentially is a condition precedent to the performance of the obligation by the Seller or Employer secured by the guarantee of the counter performance by the Buyer or Contractor by the performance bond. Is the guarantor or Insurance Company or Bank obliged to pay on demand by the beneficiary per se? This is discussed in the precedents of **Edward Owen Engineering Ltd v Barclays Bank International Ltd** case (supra); **Gold Coast Ltd versus Caja de Ahorros del Mediterraneo and others [2002] 1 All ER 142, United City Merchants (Investments) Ltd and others v Royal Bank of Canada and others [1982] 2 All ER 720** and the discussions by **Geraldine Mary Andrews and Richard Millet** in the textbook on the **Law of Guarantees Second Edition 1995 at page 444**.

The issue is also resolved by considering clause 1 of exhibit P10 which guarantees proper and faithful obligations of the "said Clause of the Contract, in the amount of USD. 3,627,762.00 (United States Dollars three million, six hundred twenty seven thousand sixty two only.)". While the Plaintiff's counsel submitted that the clause 1 of exhibit P10 dealt with obligations in the contract and which included past obligations incurred before 16<sup>th</sup> November 2012 when the APG was issued, I conclude that this cannot be. This is because of the use of the phrase cited above: "Said clause of the contract." A contextual interpretation relates to clause 2 of exhibit P2 which clearly envisages advance payment made by the Contractor (Read agent of the Employer) against an Advance Payment Guarantee to be secured thereafter. Moreover the APG would be a condition precedent as demonstrated above.

To wind up on the relevant legal principles, according to the **Geraldine Mary Andrews and Richard Millet** in the textbook on the **Law of Guarantees Second Edition 1995 at page 444**, the essential character of a performance bond is defined in the following words:

"The essential character of the performance bond is more akin to a promissory note than to a true guarantee. It is an undertaking to pay a specified sum to the beneficiary in the event of a breach of contract, rather than a promise to see to it that the contract will be performed. Similarly, the obligations of the bank or other financial institution which issues the performance bond are much more analogous to obligations arising under a letter of credit than to those arising under a guarantee."

Osborn's Concise Law Dictionary seventh edition at page 306 defines a performance bond as follows:

"A bond agreed with a creditworthy third-party, e.g. a bank, to ensure completion of contract works. It is common in construction projects. The bondholder undertakes to pay an employer a sum of money on default in completion of works by a contractor."

The cited legal doctrine points to the securing of a bond as a condition precedent to the performance of the obligations of the beneficiary under the relevant contract. The security is obtained by the other person who is to receive something whether goods or other valuable consideration from the beneficiary of the performance bond or irrevocable letters of credit or undertaking in the guarantee. Last but not least I have considered the doctrine in relation to obligations of a guarantor and when the guarantor can avoid the obligation. According to **Halsbury's Laws of England Volume 41 Fourth Edition Re-issue Paragraph 377** the general rule is discussed as follows:

"A performance bond or guarantee, only provides for payments to be made on the mere demand of the beneficiary, particularly the buyer under the contract of sale and consequently acts as an incentive to the seller to perform his obligations under the contract of sale."

The summary is that the bond is an incentive to the seller to perform his obligations. In this particular case, the defendants have raised the obligation that the seller or the Employer in this case who is the plaintiff envisaged as the beneficiary did not perform any obligations under the contract exhibit P2. The obligation as I have noted above is the payment of an advance amount of US\$3,627,762 against the Advance Payment Guarantee issued by the defendant. **Halsbury's laws of England paragraph 377** (supra) also notes that the bond or guarantee is conclusive evidence as between the bank and the beneficiary and of the beneficiary's entitlement to recover under the guarantee of the bond (See footnotes). Where, however, the bond or guarantee provides that the beneficiary is entitled to payment in certain stipulated circumstances, it has been held that the beneficiary must, when making the demand for payment, commit himself to claiming that the stipulated event has occurred. This is digested from the case of *ESAL (COMMODITIES) LTD AND RELTOR LTD v. ORIENTAL CREDIT LTD. AND WELLS FARGO BANK N.A. BANQUE DU CAIRE S.A.E v. WELLS FARGO BANK N.A.* [1985] 2

Lloyds Report 546 at pages 549 and 550. It is the holding on appeal to the Court of Appeal of Britain per Ackner, Neil and Glidewell, L.JJ. The issues considered are set out at page 549 in the judgment of Ackner LJ and is based on the contention that liability under the performance bond was conditional and the condition had not been complied with. It was contended that there was no liability under the performance bond because unless and until there had been a breach of the underlying contract of sale, and this was never established. Alternatively it was contended that the beneficiary of the performance bond not only had to make a written demand for payment under and pursuant to the performance bond, but he must in the making of the demand assert that the demand was made because the supplier had failed properly to execute the contract. The honourable judge went on to hold as follows:

“As regards the first interpretation, Mr. Tugendhat is obliged to accept if he is right, the bank by entering into the performance bond is taking upon itself the obligation of deciding the merits of the dispute under a contract of sale, the function of which it is virtually common ground the bank is wholly unfitted and which the parties could not sensibly have intended. As Mr. Sumpton for WF correctly submitted, if the performance bond was so conditional, then unless there was clear evidence that the seller admitted that he was in breach of the contract of sale, payment would never safely be made by the bank except on a judgement of a Competent court of jurisdiction and this result would be wholly inconsistent with the entire object of the transaction, namely to enable the beneficiary to obtain prompt and certain payment. There is no need to cite, at length, the well-known case of Edward Owen Engineering Ltd versus Barclays Bank International Ltd... As to the general nature of a performance bond, where it is stressed that a bank is not concerned in the least with the relations between the supplier and customer nor with the question whether the supplier has performed his contractual obligation or not, nor with the question whether the supplier is in default or not, the only exception being where there is clear evidence both of fraud and the bank’s knowledge of that fraud. See in particular the decision of this court in the United Trading Corporation SA versus Allied Arab Bank Ltd....

However, I accept Mr. Tugendhat’s alternative submission that in addition to the beneficiary making the demand, he must also inform the bank that he does so, on the basis provided for in the performance bond itself. This interpretation not only gives the meaning and effect to the words "in the event that the supplier fails..." Which otherwise would be mere surplusage, but in no way imposes an extravagant demand upon the bank. *A beneficiary may seek, honestly or dishonestly, to apply a performance bond to the wrong contract, and the need to inform the bank of the true basis upon which he is making the demand may be salutary.* Moreover, the desire for an extension of the performance bond may, on occasion, be due to the fact that the performance, for one reason or another, might have been justifiably delayed and the beneficiary does not yet

know whether or not there will in due course be full compliance with the contract. The requirement that he must, when making his demand for payment in order to support his request for an extension, also commit himself to claiming that the contract has not been complied with, may prevent some of the many abuses of the performance bond procedure that undoubtedly occur...." (Emphasis added).

The above decision was as cited with approval by the House of Lords in **Trafalgar House Construction (Regions) Ltd vs. General Surety and Guarantee Co Ltd [1995] 3 All ER 737** as an illustration of "on demand" bonds. The decision had turned both on the construction of the performance bond instrument and on general principles as quoted above.

In **Trafalgar House Construction (Regions) Ltd vs. General Surety and Guarantee Co Ltd [1995] 3 All ER 737**, the case summary is that the plaintiff contractors entered into a contract with a local authority for the construction of a leisure complex. The plaintiff's engaged sub-contractors for ground works and required them to provide a bond for 10% of the sub-contract value of £1,012,851.31. The sub-contractors entered into such a bond with the defendants, described as 'the surety', under which the surety's obligation was null and void if the sub-contractors fulfilled the terms of the contract or if on default by the sub-contractors the surety 'shall satisfy and discharge the damages sustained by' the main contractors up to the amount of the bond. Before they completed work under the sub-contract the sub-contractors went into receivership and were unable to continue. The plaintiffs completed the works themselves and issued a writ against the defendants claiming £101,285 under the bond and applied for summary judgment. The official referee refused the defendants leave to defend and entered summary judgment. The defendants' appeal to the Court of Appeal was dismissed on the grounds (i) that the purpose of the bond was to provide immediate funds for the plaintiffs in the event of failure of performance by the sub-contractors, (ii) that the bond was not a guarantee in the ordinary sense whereby the guarantor agreed to 'see to it' that the subcontractors' obligation would be performed but imposed on the surety an independent obligation to pay, on demand being made in good faith by the plaintiffs, a gross sum of damages representing the additional expenditure incurred by the plaintiffs as a result of the sub-contractors' breach and (iii) that in calculating that sum no account was to be taken of debts and credits, including the value of any set-offs and counterclaims due to or by the parties. The defendants appealed to the House of Lords.

Among the principles applied by the House of Lords is that of construction of the performance bond to establish the intention of the parties.

All that was required to activate the performance bond was a demand by the creditor stated to be on the basis of the event specified in the bond. Lord Jauncey of Tullichettle considered the wording of the bond at page 743 said:

“In recent years there has come into existence a creature described as an ‘on demand bond’ in terms of which the creditor is entitled to be paid merely on making a demand for the amount of the bond. An example of such a bond is to be found in *Esal (Commodities) Ltd v Oriental Credit Ltd, Banque du Caire SA v Wells Fargo Bank NA* [1985] 2 Lloyd’s Rep 546 at 546:

‘We undertake to pay the said amount on your written demand in the event that the supplier fails to execute the contract in perfect performance ...’

All that was required to activate it was a demand by the creditor stated to be on the basis of the event specified in the bond.”

At page 745 he said:

“There is no doubt that in a contract of guarantee parties may, if so minded, exclude any one or more of the normal incidents of suretyship. However if they choose to do so clear and unambiguous language must be used to displace the normal legal consequences of the contract—language such as was used in *Hyundai Shipbuilding and Heavy Industries Co Ltd v Pournaras* [1978] 2 Lloyd’s Rep 502 where the letter of guarantee provided—

‘the [defendant] hereby irrevocably and unconditionally guarantees the payment in accordance with the terms of the contract of all sums due or to become due by the buyer to you under the contract and in case the buyer is in default of any such payment the [defendant] will forthwith make the payment in default on behalf of the buyer ...’

This was construed as enabling the shipowner to recover from the guarantors of the buyers the amount due irrespective of the position between yard and buyers (see [1978] 2 Lloyd’s Rep 502 at 508 per Roskill LJ).”

In this suit the question for consideration primarily is what the basis of the demand is. In general it should be the default specified in the bond which is the “insurable risk”. The interpretation of the bond demonstrates that the bond or Advance Payment Guarantee envisaged related to a clause of exhibit P2 where NH – MKP Builders Ltd undertook to pay an advance payment to MKP Builders SDN BHD Ltd against an Advance Payment Guarantee. For emphasis the wording of the APG is as follows:

“In accordance with the provisions of the Contract referenced above, in relation to Advance Payments of the above-mentioned contract, MKP Builders SDN BHD Ltd of PO Box 9421, Kampala (hereinafter called "Contractor") shall deposit with the Employer an Insurance Guarantee to guarantee proper and faithful performance of the obligations

imposed by the said Clause of the Contract, in the amount of US\$3,627,762 (United States Dollars three million, six hundred twenty seven thousand sixty two only.)”

The words ‘in relation to the above mentioned contract’ refer to subcontract exhibit P2. It is not just a clever concealment of the Plaintiff as to whether it can be read as any advance payments under the main contract before or after the issuance of the APG. This is because the Plaintiff claims that the advance payments under the contract had been made. However, when the wording of the obligations of MKP Builders SDB BHD Ltd is considered, it can only come about in the subcontract exhibit P2. The only obligations of MKP Builders SDN BHD Ltd of PO Box 9421, Kampala arose in the contract it had with NH – MKP Builders Ltd in exhibit P2. It is stretching the language of the contract document to imply that advances under the contract mean advance payments made under the Main Contract exhibit P1. MKP Builders SDN BHD Ltd of PO Box 9421, Kampala was only entitled to advance payment under exhibit P2 and clause 2 thereof even if its obligations include obligations to implement the main contract between NH – MKP Builders Ltd and National Housing and Construction Company Ltd.

Secondly the phrase “Clause of the Contract, in the amount of US\$ 3,627,762” when read in context of other factors refers to clause 2 of exhibit P2 under which MKP Builders SDN BHD Ltd of PO Box 9421, Kampala was entitled to receive an advance payment against security of an APG. Clause 2 of exhibit P2 provided that:

"The Contractor hereby undertakes to pay the Subcontractor 20% of the contract sum as advance payment against receipt of an advance payment guarantee from a Bank or Insurance Company that is acceptable to the Contractor, and in the amount and currency equal to the advance payment."

The wording of clause 2 of exhibit P2 gives the context of the expected payment under the APG which was issued to secure payment: “against receipt of an Advance Payment Guarantee from a Bank or Insurance Company that is acceptable to the Contractor and in the amount and currency equal to the advance payment”

In the absence of the payment then there was a vital condition precedent which had not been met by the beneficiary. The beneficiary did not do what was required by the security which was to make advance payment to the subcontractor through the agency of NH – MKP Builders Ltd under exhibit P2. The problem is made more complex by the simple fact that the Plaintiff is not a party to exhibit P2 and neither is the Defendant. Because of that it may be contended on the basis of judicial precedents cited above that only the performance bond exhibit P10 should be read and the defendant is not concerned with the relationship between the Plaintiff (who is the beneficiary intended to be paid in the APG and MKP Builders SDN BHD who are the persons who procured the APG under the contract exhibit P2). Secondly the demand which was made by the plaintiff conceals the fact that MKP builders SDN BHD Ltd was not paid any advance after 16<sup>th</sup> of



November 2012. The demand is dated 4<sup>th</sup> of February 2013 and it is written in part there under as follows:

"Reference is made to the Advance Payment Guarantee for the construction of 312 condominium apartments split into 12 blocks each 4 floor. Each unit is approximately 135 (meters squared) split between two floors inclusive of preliminaries and contingencies in the Naalya Pride Project, a copy of which is attached.

Please note that MKP Builders SDN BHD Ltd has failed to implement the said construction contract. Furthermore the recovery of the advance payment made by National Housing has not been possible because of the failed contract.

This is to formally demand that you satisfy/pay the guarantee amount of USD 3,627,762 to the Employer; National Housing and Construction Company Ltd in the current bank account number 0121110015801 held with Housing Finance Bank.

We appreciate your early response.”

The first point to be noted is that the advance payment guarantee in question was issued on 16<sup>th</sup> November, 2012. This demand is dated 4<sup>th</sup> of February 2013 about 2 ½ months later. Because the APG is a condition precedent to the fulfilment of obligations of NH MKP Builders Ltd under exhibit P2, no advance payment had been made between 16<sup>th</sup> November 2012 and 4 February 2013 while the demand of the plaintiff implies that an advance payment had been made. The fact that NH - MKP Builders Ltd was advanced money by the Plaintiff earlier on is not relevant to the construction of exhibit P2 or P10. Under exhibit P2 advance payment if made by NH – MKP Builders Ltd to MKP Builders SDN BHD of Malaysia as the subcontractor. This payment could only be made against an APG issued and deposited with the Plaintiff.

However in terms of strict construction of exhibit P10 which is the APG in question, the advance payment should be made after the security was created and not before. The Plaintiff clearly and unequivocally notified the Defendant in the demand note that reference was made to the Advance Payment Guarantee for the construction of 312 Condominium Units. Secondly, it is written in paragraph 3 of the demand letter as follows:

“Please note that MKP Builders SDN BHD Ltd has failed to implement the said construction contract. Furthermore the recovery of the advance payment made by National Housing has not been possible because of the failed contract.”

The Defendant was notified in that paragraph that recovery of the advance payment made by National Housing had not been possible because the contract failed. Can the defendant not ask which Advance payment? The Plaintiff was under a duty to disclose the advance payment it made and the breach of the contract to the Defendant.

Following my extensive discussion of the issue above, the advance payment in exhibit P2 would only be made against an advance payment guarantee which had been issued and had to be made after the advance payment guarantee had been issued or secured by the Subcontractor. It follows that the information in the demand was deceptive because it concealed the fact that no advance payment had been made against the APG issued by the defendant. Instead it was an advance payment which had been made before the issuance of the APG exhibit P10 of 16<sup>th</sup> November 2012. I therefore I agree with the interpretation of the defendants counsel and the evidence of DW1 and DW2 that the demand was fraudulent because it is based on an earlier advance made before the defendant came on-board. Last but not least the last paragraph of the advance payment guarantee exhibit P10 speaks for itself. It provides that:

“This guarantee shall remain valid and in full effect from the date of the advance payment under the contract until the employer receives full repayment of the same amount from the contractor but in any case not later than 26/12/2013.”

The phrase in the above quotation "advance payment under the contract" can only be construed to mean an advance payment which had been made against the APG issued by the defendant on 16<sup>th</sup> of November 2012. This is because the advance payment is that under clause 2 of exhibit P2. All other advance payments which could have been made were not secured by the defendant and the bond issued by the defendant cannot be used as security therefore. In the premises I do not have to consider any other advance payment on the basis of the legal doctrine discussed above.

On the above ground alone, issue number one as to whether there was any advance payment made against the guarantee dated 16<sup>th</sup> of November 2012 is answered in the negative. It follows that issue number two of whether the defendant is liable to pay the plaintiff any money under the advance payment guarantee dated 16<sup>th</sup> of November 2012 is also answered in the negative for failure of the condition precedent to the payment under the APG.

In the premises, there is no need to consider other issues and matters submitted on because it is my conclusion pursuant to the above that the plaintiff's suit lacks merit and is hereby dismissed with costs.

Judgment delivered in open court on the 17<sup>th</sup> of February 2017

**Christopher Madrama Izama**

**Judge**

Judgment delivered in the presence of:

Counsel Isaac Walukagga for the Plaintiff

*Decision of Hon. Mr. Justice Christopher Madrama Izama \*^\*~ \*&\*\$\$# xtra+ maximum735securityx 2017 style*

Counsel Sophie Nyombi holding brief for Earnest Kalibala and Frederick Nyombi for the Defendant

Charles Okuni: Court Clerk

Julian T. Nabaasa: Research Officer Legal

**Christopher Madrama Izama**

**Judge 17/02/2017**