IN THE HIGH COURT OF KENYA AT NAIROBI

MILIMANI LAW COURTS

COMMERCIAL AND TAX DIVISION

CORAM: D. S. MAJANJA J.

CIVIL CASE NO. E186 OF 2020

BETWEEN

GLOBE DEVELOPERS LIMITED.....PLAINTIFF

AND

MAYFAIR INSURANCE COMPANY LIMITED.....DEFENDANT

RULING

Introduction

1. There are two applications for consideration in this ruling. The first is the Plaintiff's application dated 25th June 2020 made under **Order 36 rule 1** of the ***Civil Procedure Rules*** seeking summary judgment against the Defendant for Kshs. 143,430,335.00 together with interest thereon until payment in full. It is supported by the affidavit and further affidavit of its director, Abdul Kasmani. The application is opposed by the Defendant through three replying affidavits sworn on 30th July 2020 by Emma Mwangi, its Legal Manager, Dinesh Sampathirao, an Engineer employed by Mark Properties Limited and Kigo Kariuki, Chief Executive Officer of Safety Surveyors Limited.

2. The second application is the Defendant's application dated 6th August 2020 seeking to strike out the Plaint made, inter alia, under **Order 2 rule 15(1)(b), (c) and (d)** of the ***Civil Procedure Rules*** on the grounds that it is an abuse of the Court process and that it is scandalous, frivolous and vexatious. It is supported by the affidavits of Emma Mwangi, Dinesh Sampathirao and Kigo Kariuki all sworn on 6th August 2020. It is opposed by the Plaintiff through its Grounds of Opposition dated 14th August 2020 as well as the replying affidavit of Abdul Kasmani sworn on the same date.

Background and Pleadings

3. The facts leading to the dispute are largely common cause and can be gleaned from the Plaint dated 4th June 2020, the Defence dated 7th July 2020 and the various depositions sworn on behalf of the parties.

4. The Plaintiff is the registered proprietor of LR No. 209/4904 situated at Riverside Gardens, Riverside Drive Nairobi ("the suit property"'). Through an agreement, a Joint Building Contract dated 10th July 2016 ("the Contract"), it engaged Mark Properties Limited ("the Contractor") to construct a 19 storey apartment block on the suit property. Under the Contract, the Contractor was required to provide a surety from either an established bank or an insurance company approved by the Plaintiff who would be bound to the Plaintiff in the sum equivalent to ten per cent of the contract price for the due performance of the Contract.

5. On 19th August 2016, the Defendant issued a performance bond ("the Bond") in favour of the Plaintiff for the due performance by the Contractor of the Contract in the sum of Kshs. 143,430,335.00. The Bond was valid from 9th July 2016 to 22nd February 2020.

6. The construction was to commence on 1st July 2016 and the date of practical completion was 17th May 2019. On 17th May 2019, the construction was incomplete and the Architect sent to the Contractor a Notice of Default giving the contractor 14 days to remedy the defects as contained in the Notice of Default. As the Contractor failed to remedy the defects, the Plaintiff terminated the Contract by its letter dated 7th June 2019. Subsequently and by a letter of demand dated 7th June 2019 addressed to Defendant, the Plaintiff, through its advocates, demanded forfeiture of the Bond. As the Defendant failed to honour the demand, the Plaintiff filed this suit seeking the value of the Bond.

7. The Defendant resisted the suit. In its Defence dated 7th July 2020, it admitted that it issued the Bond for the validity period. It stated that the Bond provided that any alteration to the terms of the Contract, or in extent of the nature of the works to be carried out, or any extension of the time would release it from liability and since there were alterations in the nature and extent of works, it was discharged from any liability under the Bond. It further contended that it was not possible to determine whether any liability arose from the Bond as there was a dispute between the Plaintiff and the Contractor which is still pending before an arbitral tribunal.

8. The Defendant admitted that it received the demand letter but denied that the Plaintiff was entitled to payment as it had made material alterations to the Contract. It also stated that the suit was filed outside the Bond validity period.

The applications and general principles

9. The parties through their advocates filed written submissions in support of their respective positions. The law applicable to the applications is not controversial at all and has been settled in several cases. In dealing with both applications, the court is guided by the general principle that it should be circumspect in striking out the plaint or entering summary judgment unless there are clear grounds to do so.

10. The court's power to strike out pleadings is to be exercised sparingly and cautiously as was held by the Court of Appeal in ***D.T. Dobie & Company (Kenya) Ltd v Muchina*** **[1982] KLR 1** where it stated as follows:

> ***No suit ought to be summarily dismissed unless it appears so hopeless that it plainly and obviously discloses no reasonable cause of action and is so weak as to be beyond redemption and incurable by amendment. If a suit shows a mere semblance of a cause of action, provided it can be injected with real life by amendment, it ought to be allowed to go forward for a court of justice ought not to act in darkness without the full facts of a case before it.***

11. Likewise, and as regards summary judgment, the Court of Appeal in ***Job Kilach v Nation Media Group Ltd, Salaba Agencies Ltd & Michael Rono*** **[2015] eKLR** observed that:

> *Before the grant of summary judgment, the court must satisfy itself that there are no triable issues raised by the defendant, either in his statement of defence or in the affidavit in opposition to the application for summary judgment or in any other manner. What then is a defence that raises no bona fide triable issue? A bona fide triable issue is any matter raised by the defendant that would require further interrogation by the court during a full trial. The Black's Law Dictionary defines the term* ***"triable"*** *as,****"subject or liable to judicial examination and trial."*** *It therefore does not need to be an issue that would succeed, but just one that warrants further intervention by the Court.*

12. The dispute in this matter implicates the nature of the performance bond and its legal implications. Both counsel have submitted extensively and cited authorities to support their respective positions which I shall now consider.

13. According to ***Black's Law Dictionary*** **(10th Ed)** a performance bond is, *"A bond given by a surety to ensure the timely performance of a contract"* and *"A third party's agreement to guarantee the completion of a construction contract upon the default of the general contractor"*. It is common ground that a performance bond is a separate and distinct agreement from the underlying agreement (see ***Sinohydro Corporation Limited v GC Retail Limited and Another*** **[2016] eKLR** and ***Gatare Limited v Standard Assurance Kenya Limited*** **HCCC No. 254 of 2008 [2009] eKLR**).

14. A performance bond has been likened to letters of credit and guarantees. In ***Kenindia Assurance Company Limited v First National Finance Bank Limited*** **NRB CA Civil Appeal No. 328 of 2002 [2002] eKLR**, the Court of Appeal cited with approval the following dicta of Lord Denning in ***Edward Owen Engineering Ltd v Barclays Bank International Ltd*** **[1978] ALL ER 976**;

> *All this leads to the conclusion that the performance guarantee stands on a similar footing to a letter of credit. A bank which gives a performance guarantee must honour that guarantee according to its terms. It is not concerned in the least with the relations between the supplier and the customer, nor with the question whether the supplier has performed his contracted obligation or not; nor with the question whether the supplier is in default or not. The bank must pay according to its guarantee, on demand if so stipulated, without proof or conditions. The only exception is when there is clear fraud of which the bank has notice.*

15. The same position was summarized in ***Transafrica Assurance Co. Ltd v Cimbria (EA) Ltd*** **[2002] 2 EA 627 (CAU)**, where it was held that:

> *A performance bond has many similarities to a letter of credit and it has long been established that when a letter of credit is issued and confirmed by a bank, the bank must pay it if the documents are in order and the terms of credit are satisfied. Any dispute between a buyer and seller must be settled between themselves and the bank must honour the credit ……..... A bank or institution giving a performance bond is therefore bound to honour it in accordance with the terms of the bond if it appears the papers are in order regardless of any dispute between the buyer and the seller arising from the contract in respect of which the bond was given. It is only excused where there is fraud of which it has notice.*

16. It is against this background and the following uncontested facts that the applications are to be resolved. First, the Defendant issued the Bond in favour of the Plaintiff. Second, the Contractor failed to perform its obligations under the Contract whereupon the Plaintiff terminated it and lastly, upon termination, the Plaintiff issued a demand to the Defendant calling for liquation of the Bond. This suit has been precipitated by the Defendant's failure to comply with the demand.

17. As the Defendant has admitted the Bond, it bears the burden of showing why it seeks to avoid settlement of the Bond. In its statement of defence, the Defendant raised the following issues which I shall consider in light of the applicable principles:

(a) Whether the suit is barred.

(b) Whether alterations or variations to the Contract discharged the Defendant's obligations under the Bond.

(c) Whether the payment under the Bond is subject to arbitration proceedings between the Plaintiff and the Contractor.

Bond validity period

18. The Defendant submitted that this suit was presented outside the Bond validity period hence the Plaintiff is not entitled to payment. The Bond was valid from 9th July 2016 to 22nd February 2020. Since the suit was filed on 5th June 2020, it contended that the Plaintiff is barred from taking these proceedings to enforce the Bond as the Defendant was discharged from liability once the Bond had expired. It relied on the case of ***China Civil Engineering Corporation v Capitaland East Africa Limited and Stanbic Bank Kenya Ltd*** **HC COMM No. 228 of 2019 [2020] eKLR**.

19. The Plaintiff responded that the demand letter dated 7th June 2019 calling up the Bond was sent to the Defendant during the bond validity period. It submitted that it is the failure by the Defendant to pay up the bonded sum that necessitated the commencement of the present suit. It added that the suit can be commenced within 6 years from the date of the contractor's default so long as the demand is made within the bond validity period.

20. Counsel for the Plaintiff cited the decision of the Court of Appeal in ***Kenindia Assurance Company Limited v First National Finance Bank Limited*** **(Supra)** which resolved this issue as follows:

> *In the summary judgment application, the learned trial Judge was satisfied that the appellant executed the guarantee, it had been notified in time about default on the part of Universal Apparels [EPZ] Ltd, and that a demand had been made before the expiry date of the guarantee. The issue which dominated submissions by counsel in the superior court was whether the respondent had exhausted "all avenues of recovery directly from the principal" and also whether as at the date the demand was made the guarantee was valid. It is in evidence that the respondent advised the appellant of the default by the principal debtor by a letter dated 28th June 1997. The letter of demand is dated 18th August 1997 and was received by the appellant on the same day. The expiry date of the guarantee was 27th August 1997. It is our view that as at the date the demand was made the guarantee had not expired and was therefore still valid.*

21. As it is not disputed that the demand was made within the bond validity period, it is a valid demand particularly in light of the authoritative and binding decision of the Court of Appeal. The case of ***China Civil Engineering Corporation v Capitaland East Africa Limited and Stanbic Bank Kenya Ltd*** **(Supra)** relied on by the Defendant is easily distinguishable as it was in respect of an application to set aside a judgment whose effect would have amounted to reinstating a guarantee that had already expired.

Whether the Defendant is discharged

22. The Defendant submitted that irrespective of the contractual rights under the Contract, the Plaintiff has a contractual obligation under the Bond to disclose any variation made to the scope of the works in the Contract. Consequently, it submitted that the Plaintiff is not entitled to payment due to the fact that it made several alterations to the scope of works under the Contract.

23. The Defendant relied on the depositions of Emma Mwangi, Dinesh Sampathirao and Kigo Kariuki to show that the following alterations were made to the works:

§ The tiling works, wardrobes, kitchen cabinets and granite works and doors (including door frames) set out in the Contract were removed from the Contractor's scope of works.

§ Several changes were made to architectural drawings made by the Architect.

§ The diameter of the right hand side railing was changed from 75mm to 50mm.

§ The height of the passage railing changed from 90mm as set out in the Bill of Quantities to 1,200.

§ A gypsum ceiling above the walkway was added to the Works;

§ A beam along the grid C (7,8) was moved towards grid B.

§ The passage of the solar water hearing pipes in blocks A, B and G was changed and covered with gypsum.

§ The changing rooms at level 5 were re-located from the original position to create, inter alia, additional parking space.

§ Cutting the slab family room slab to allow an open staircase within the duplexes.

§ The main staircase was changed to include masonry railing.

§ New garden slabs were included.

§ Privacy screens were added to the 4 bedroom units in block D and E.

§ RC walls were included to the children's play area.

§ A new staircase was to be included on level 0 in Block E and F.

24. The Defendant contended that alterations outlined were outside the scope of works under the Contract and it was therefore released from any liability under the Bond. In his deposition, Kigo Kariuki stated that the Plaintiff failed to communicate to the Defendant any of the variations made to the Contractor's scope of works under the Contract thus denying the Defendant the opportunity to re-assess the valuation of the project to adequately reflect the variations made to the scope of work. The Defendant submitted that under the law of insurance and in particular the principle of utmost good faith, the Plaintiff has a duty to disclose any information that could adversely affect the insurance contract. The Defendant therefore submitted that the Plaintiff was in breach of the duty of good faith and disclosure by denying the Defendant the right to re-assess the insured sum under the Bond.

25. Counsel for the Defendant cited ***David Harris v Middle East Bank Kenya Limited and 3 Others*** **NRB CA Civil Appeal No. 34 of 2011 [2019] eKLR** to support the proposition that alteration of guaranteed obligations releases the guarantor from liability and that a guarantor will be discharged from liability under a guarantee where material alterations are made to the underlying contract. In this case, the Defendant argued that the variation permitted under the Contract did not apply to the Bond since the obligation under both agreements are separate and distinct and even if the Architect was permitted to make the variations then the Plaintiff ought to have notified the Defendant.

26. The Plaintiff argued that although the Bond provided that alteration in the terms of the contract or in the extent or nature of the works to be carried out and by extension of time by the Architect under the contract would release the surety from liability, in this case there were no alterations to the terms of the contract nor extension of time by the Architect under the Contract.

27. In response to the Defendant's contention that the Plaintiff had made alterations, it submitted that the Contract, particularly Article 30.0 thereof, provided for and permitted certain variations authorised by the Architect. It pointed out that any alterations made to the construction as set out in the Defendants depositions were made by the Architect as envisaged in the contract and did not amount to alterations of the extent or nature of the works carried out. The Plaintiff further submitted that Defendant had not shown that the modifications complained of went beyond the scope of variations allowed by the Contract and the Defendant cannot avoid liability in this regard. It maintained that the nature and extent of the works to be carried out had not changed as what was to be built was the Duplex Apartments on Plot LR No. 209/4904, Nairobi, 9 Blocks Ranging from 12 Storey to 19 Storey Including a basement of 5 Floors and this is what the Defendant agreed to under the Bond.

28. The relevant part of the Bond necessary for resolution of this issue states as follows:

> *PROVIDED always and it is hereby agreed and declared that any alteration in the terms of the said contract or in the extent or nature of the works to be carried out and any extension of time by the Architect under the contract shall in all ways release the surety from any liability under the above written bond.*

29. From the aforesaid provision, the surety will be discharged and released from liability on any three of the following grounds; First, alteration in any terms of the Contract. Second, alteration in the extent or nature of the works to be carried out and lastly, extension of time by the Architect.

30. The issue raised by the Defendant is whether the alterations, outlined at para. 24 above, carried out in the nature and extent of the works discharged the Defendant from liability under the Bond. The Plaintiff does not dispute that alterations were carried out but contends that they were contemplated and covered by Clause 30 of the Contract which provides as follows:

> *30.1 The term 'variation' as used in these conditions shall mean the alterations or modifications of the design, quality or quantity of the works as shown upon the contract drawings and described by or referred to in the contract bills and specifications and includes;*
>
> *30.1.0 The addition, omission or substitution of any item of work.*
>
> *30.1.2 The alteration of the kind or standard of any of the materials or goods to be used in the works.*
>
> *30.1.3 The removal from the site of any work, materials, or goods brought upon the works by the contractor for the purposes of the works other than work, material or goods which are not in accordance with the contract.*
>
> *30.1.4 The issue of instructions by the architect in regard to the expenditure of prime cost and provisional sums included in the contract bills and of prime cost sums which arise as a result of instructions issued in regard to the expenditure of provisional sums.*
>
> *30.2 …*
>
> *30.3 If the net value of all variations should equal 15% of the builders work, the Architect shall not issue any further instructions requiring a variation for additional work without the consent of the Employer and Contractor.* [Emphasis mine]

31. The aforesaid clause in the Contract is clear and I find that variations approved by the architect are contemplated and provided and it is only if they exceed 15% of the builder's work that the Employer and Contractor are required to consent. Further, under the terms of the Bond, the Defendant guaranteed that the Contractor would, *"carry out and complete the work therein stated in the manner and by the time therein specified all in the accordance with the provisions of the said contract namely; PROPOSED DULEX APARTMENTS ON PLOT LR. NO. 209/4904, NAIROBI, 9BLOCKS RANGING FROM 12 STOREY TO 19 STOREY INCLUDING OF 5 FLOORS."*

32. I therefore agree with the Plaintiff that as long as the variations were within the Contract, the Bond was not thereby discharged. Counsel for the Plaintiff cited ***Keating on Building Contracts*, (5th Ed, 1991) at page 252-253** which states;

> *Any material alteration of the obligation guaranteed releases the surety. Thus extending the time for performance releases a surety for completion, unless there is an express provision for the extension of time… It is submitted that on general principles a material variation of the contract works, not within the scope of a clause permitting the ordering of variations, discharges the surety. (Emphasis mine)*

33. I have considered the variations outlined by the Defendant and it is evidence that they do not depart from the scope of work defined by the Contract. The variations include the use of different material, replacement and substitution of certain items with others and re-design or modification of the designs all falling within Clause 30 of the Contract and therefore valid. It is not alleged either by the Contractor or the Defendant that the variations breached the Contract in the manner contemplated by Clause 30.

34. The Defendant also relied on the doctrine of utmost good faith in insurance contracts to support its argument that the Plaintiff had a duty to inform it of any variation under the Contract. I reject the contention that the principle of utmost good faith is applicable to a performance bond. In doing so, I would do no better that state what the Court of Appeal held in ***Corporate Insurance Co. Ltd v Nyali Beach Hotel* [1995-1998] 1 EA 7** as follows:

> *[In a performance bond] The risk taken is generally known to the surety and the circumstances generally point to the view that as between the creditor and surety it was contemplated and intended that the surety should take upon himself to ascertain exactly what risk he was taking upon himself. Ordinary contracts of guarantee are not amongst those requiring uberima fides on the part of the creditor towards the surety by the creditor of the facts known to him affecting the risk undertaken by the surety will not vitiate the contract.*

35. As the Bond is not a contract that is underpinned by the doctrine of utmost good faith, there was no obligation on the Plaintiff to disclose the variations. These variations were within the Contract provisions which the defendant knew when it issued the Bond. Unless there was an obligation in the Bond for the Plaintiff to inform the Defendant of variations in the underlying contract or seek its consent, the Defendant cannot set up this argument as a Defence and it is therefore not a triable issue.

36. The Defendant relied on the case of ***David Harris v Middle East Bank Kenya Limited and 3 Others* (Supra)**to support its position but the facts in that case are easily distinguishable. In that case, the Court of Appeal discharged the guarantors in a lending agreement after the bank varied the lending agreements several times without the consent of the guarantors by inter alia, granting additional facilities and rescheduling the terms of payment whose effect was to substantially prejudice the guarantor. The Defendant also relied on the case of ***Leo Investments Limited v Trident Insurance Company Limited* HC COMM No. 893 of 2010 [2014] eKLR** which was based on its own facts as the Contractor was specifically released from liability and consequently, the court held that the Bond was discharged.

37. I do not find any triable issues as the variation complained of were within the Contract and as such contemplated under the Bond. Further, it was not a requirement of the Bond that the Plaintiff informs the Defendant of any variations.

Existence of Arbitration proceedings

38. The Plaintiff admits that there is a dispute between it and the Contractor. Dinesh Sampathirao deponed that there are pending arbitration proceedings concerning, amongst other issues, unlawful termination of the Contract, unlawful retention of its machinery, equipment and property on the suit property and non-payment for work completed amounting to Kshs. 258,581.763.61. The Defendant contended that until the dispute is resolved, it is not possible to determine whether or not any liability arises from the Bond. It argues that the court in allowing the application will result in unjust enrichment of the Plaintiff.

39. The Plaintiff reiterated that the Bond is independent from the Contract and therefore the arbitration proceedings and the present suit can proceed concurrently. It submitted that the dispute between the Plaintiff and the Contractor has no bearing on the Bond. It further submitted that unjust enrichment cannot occur in this instance where the sums that have been secured in favour of the Plaintiff by the Bond become due and owing following the Contractor's failure to complete the Contract in the manner and time specified.

40. A dispute between the Plaintiff and Contractor as is the case here does not affect the surety's obligations as the Bond remains an independent contract. This is what the court stated in ***Edward Owen Engineering Ltd v Barclays Bank International Ltd* (Supra)** and in ***Kenindia Assurance Company Limited v First National Finance Bank Limited* (Supra)** where the Court of Appeal also held as follows;

> *A bank, which gives a performance guarantee, must honour that guarantee according to its terms. It is not concerned in the least with the relations between the supplier and the 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 bank must pay according to its guarantee, on demand if so stipulated, without proof or conditions …….. only exception is when there is clear fraud of which the bank has notice..... As to the fulfilment of the conditions incorporated in the guarantee the statement of the beneficiary shall be taken at its face value unless the contractor can establish that the beneficiary's stand is motivated by fraud, misrepresentation, deliberate suppression of material facts or the like of which would give rise to special equities in favour of the contractor.."* [Emphasis mine]

41. The Defendant has not alleged or pleaded fraud or misrepresentation in its defence. The dispute between the Plaintiff and Contractor is an ordinary dispute and the calling of the Bond is precisely meant for circumstances where the Contractor fails to perform its obligations. I therefore hold that that the existence of arbitration proceeding between the Plaintiff and its Contractor does not affect the liability of the Defendant under the Bond and is not a triable issue.

Whether Summary Judgment should be entered?

42. I have found that none of the issues raised by the Defendant in its defence raise bona fide triable issues. The condition precedent in the liquidation of the Bond is a letter of demand. The Bond provides that:

> *Upon default and without prejudice to his other rights under the contract, the Employer shall be entitled to demand forfeiture of the bond and we undertake to honour the demand in the amount stated above on the first demand in writing.*

43. Liability under the Bond has crystallised once the Plaintiff issued the demand letter dated 7th June 2019. The court therefore has no option but to enter judgment for the amount in the Bond as the Defendant's defence does not raise any bona fide triable issues.

Disposition

44. For the reasons I have set out above, I now make the following orders:

(a) The Notice of Motion dated 6th August 2020 be and is hereby dismissed with costs to the Plaintiff.

(b) The Notice of Motion dated 25th June 2020 is allowed and judgment be and is hereby entered for the Plaintiff against the Defendant for the sum of Kshs. 143,430,335.00.

(c) The said amount shall accrue interest at 12% p.a. from the date of filing the suit until payment in full.

(d) The Defendant shall pay the costs of the suit.

DATED and **DELIVERED** at **NAIROBI** this **13TH day of NOVEMBER 2020.**

D. S. MAJANJA

JUDGE

Court Assistant: Mr M. Onyango.

Ms Kamau instructed by Wandabwa and Company Advocates for the Plaintiff.

Mr Maillu instructed by LJA Advocates for the Defendant.