



**REPUBLIC OF KENYA  
IN THE HIGH COURT OF KENYA  
AT NAIROBI (MILIMANI COMMERCIAL COURTS)**

**Civil Case 593 of 2006**

**GONDHO ENTERPRISES LIMITED .....PLAINTIFF**

**VERSUS**

**CONCORD INSURANCE COMPANY LIMITED .....DEFENDANT**

**RULING**

In the plaint dated 31<sup>st</sup> October 2006, the plaintiff alleges that by an agreement dated on or about 16<sup>th</sup> May, 2005, it contracted M/S Jaswant Singh and brothers Limited, a building contractor to construct apartments to be known as Cornerstone Apartments on its land reference Number 209/363/10 Woodlands Avenue, Nairobi. It was a mutual term and conditions of contract for building works that the contractor would procure and/or furnish the plaintiff with a performance bond for 10% of the total construction amount of shs.68,500,000/= in consideration and for the due performance by the contractor of the terms of the said contract.

In compliance, the contractor did obtain a written performance bond duly executed in favour of the plaintiff from the defendant herein. The said performance bond is the one dated 24<sup>th</sup> May 2005. And upon procuring and availing the performance bond, the contractor moved to site and commenced the construction works in line with the provisions of the building contract of 16<sup>th</sup> May 2005. In the middle of the works, a dispute arose between the plaintiff and the contractor **M/S Jaswant Singh and Brothers Limited** owing to some alleged breaches committed by the contractor.

In a letter dated 9<sup>th</sup> January 2006 the plaintiff through its project architects **M/S Adventis Limited**, terminated the construction contract with the contractor. Again by a letter dated 20<sup>th</sup> February 2006 and received by the defendant on 24<sup>th</sup> February 2006, the plaintiff notified the defendant of the termination of the contract, giving the reasons for doing so. The plaintiff then demanded payment of the bond sum of Kshs.6,850,000/= being 10% of the contract amount in terms of the performance bond executed by the defendant on 24<sup>th</sup> May, 2005.

In its statement of defence, the defendant states that it was not privy to the contract subject of this dispute and cannot be bound by the terms thereof in law or otherwise. It is also contended that the contract dated 16<sup>th</sup> May 2005 is fatally defective, bad in law and unenforceable in law otherwise for failure to comply with mandatory provisions of law. It is further contended that the said contract was to be under seal but the same was breached and as such, it was void *abintio*, fatal and unenforceable.

The defendant in its defence also attacked the performance bond to be unenforceable as it was not sealed and/or written under common seal of the defendant's company or stamped with its stamp. The mandate and authority of the person who executed the document on behalf of the defendant is also questioned. It

is alleged that the said person had no authority to bind the defendant or issue the same on behalf of the defendant. And that there was no resolution for issuance of the said performance bond.

The plaintiff has now made an application dated 21<sup>st</sup> November, 2006 under Order 12 Rule 6, 35 Rules 1(1) and 5, order 39 Rule 7(1) (a) and 8 of the Civil Procedure Rules. The application is also made under sections 3A and 63(b) and (e) of the Civil Procedure Act. The prayers in the said application are;

- (1) That judgement on admissions be and is hereby entered against the defendant and in favour of the plaintiff for the sum of Kshs.6,850,000/= plus costs and interest as the court may deem fit.**
- (2) That in the alternative and without prejudice, summary judgment be and is hereby entered against the defendant in favour of the plaintiff as per the plaint herein dated 31/10/2006.**
- (3) That by way of detention and preservation of the subject matter, pending the hearing and determination of the application and/or suit herein, the principal sum of Kshs.6,850,000/= guaranteed under the suit performance bond dated 25<sup>th</sup> May 2005 on or before 30/11/2006.**

The defendant has filed a replying affidavit sworn by **Mr. Francis Irungu** on 31<sup>st</sup> January, 2007 and filed in court on 2<sup>nd</sup> February, 2007. The deponents states that he is the principal officer of the defendant company with the mandate to oversee the company's day to day operations. That he is the one authorized to be a signatory of any performance bond or guarantee on behalf of the defendant together with any of the defendant's directors.

The deponents avers that none of the defendant's directors is mandated or authorized to issue any performance bond on behalf of the defendant as a single signatory unless the document is executed by two signatories and sealed or stamped with the defendant's common seal or stamp.

And in paragraph 6 he states;

**"That I am also well aware as the defendant's chief executive officer that the defendant's board of directors had on numerous occasions passed resolutions to the effect that any performance bond or guarantee issued on behalf of the defendant must be executed by at least two directors or one director together with myself".**

And in paragraph 8 the deponent contends;

**"That I had never seen or known about the performance bond which is in issue herein and which is allegedly issued to the plaintiff by the defendant prior to the plaintiff's demand and subsequent filing of this suit".**

It is also essential to reproduce what **Mr. Irungu** states in paragraph 10 of the replying affidavit;

**"That I am advised by the defendant's counsel on record Mr. P. Munge Murage, a partner with the firm of Muriu, Mungai & co. Advocates which advise I verily believe to be true that the alleged bond is bad in law, incompetent, unenforceable and cannot bind the defendant on the grounds that;**

- (a) the alleged performance bond does not bear the defendant's seal**
- (b) The alleged performance bond bid not have any official stamp of the defendant.**
- (c) The executor of the document is doubtful**
- (d) The alleged performance bond was issued without the authority of the defendant".**

In a further affidavit filed on 22<sup>nd</sup> February 2007, the plaintiff's director **Mr. Joel Mudhune** states that as

a matter of public notice that one **Mr. C. N. Umamaheswar** the executor of the performance bond is the defendant's long-serving Executive Director. And the witness **Mr. E. Kaburu** is also a director. And that the defendant issued a protection cover note to the contractor dated 18.5.2005 for the entire contract sum in line with the practice in the construction industry. He alleges that the said policy was furnished alongside the performance bond to the plaintiff by the contractor. The deponent also exhibited another bond issued by the defendant which shows that it was signed and/or executed by **Mr. Irungu** and **Mr. C. N. Umamaheswar** both as executive directors.

It is the contention of the plaintiff that the subject bond is good and valid in law or otherwise binding and enforceable. It is also the position of the plaintiff that the defendant cannot plead and/or be allowed to take advantage and benefit from its own willful acts and/or omissions to defeat its claim which is lawful and rightful. And in the end **Mr. Joel Mudhune** terms the replying affidavit of **Mr. Irungu** as spurious, dishonest, done in bad faith replete with misrepresentations and material non disclosures, hence it has no evidential value at all.

I have considered the case of the plaintiff as against the defence put forward by the plaintiff. I have also taken into consideration the affidavits presented by both parties as regards the application under my determination. And it suffices to say the central issue is the performance bond dated 24<sup>th</sup> May, 2005. It concerns what was referred to as the proposed Cornerstone apartment on plot No.209/363/10, **Woodlands Avenue**, in Nairobi. The performance bond was preceded by a contract dated 16<sup>th</sup> May 2005 between the plaintiff herein and a contractor by the name **Jaswant Singh and brothers Limited**. The said contractor was engaged to undertake or construct apartments known as Cornerstone apartments on the applicant's property. The contract price was Kshs.68,500,000/= and it stipulated that the contractor to provide as a condition precedent for its due performance in the form of a surety and/or performance bond of Kshs.6,850,000/=.

In essence the contractor was obligated to procure and furnish the applicant with a performance bond for 10% of the contract value in consideration towards the due performance, by the contractor of the terms of the said contract. On its part the plaintiff was required to provide to the contractor with all available date and information regarding the site and surrounding circumstances, whilst the contractor was equally deemed to have obtained all relevant information and satisfied itself on the correctness and sufficiency of the tender for the subject construction works.

The document that was signed between the plaintiff herein and the contractor contains an exhaustive regime of rights and remedies to the parties in the event of default or breach by either party. The contractor as was required did secure from the defendant and furnish to the plaintiff herein a performance, bond dated 24<sup>th</sup> May, 2005 in compliance with his contractual obligation. It is pertinent to note that the plaintiff was not involved in the preparation and execution of the said performance bond. And when it was given to him as a condition precedent for the construction agreement to take place, it duly and readily accepted. The details and manner of execution was an issue between the contractor and the defendant herein. It is essential at this stage to note that the performance bond created a relationship and/or obligation between the plaintiff and defendant that is completely different and/or independent from the relationship between the defendant and the contractor.

In my view the basis of the contractor providing a performance bond was to aid him get and/or secure the construction contract. It means the performance bond was provided in satisfaction of the preliminary obligation placed on the contractor so that it could start the construction works on behalf of the plaintiff.

No doubt the defendant issued an interim protection cover note on 18<sup>th</sup> May, 2005 to enable the contractor to move to the site and commence the works pending the processing and issuance of the ultimate performance bond dated 24<sup>th</sup> May, 2005, which is exhibited in the plaintiff's further affidavit as JM2. Upon issuance of the performance bond, the surety would in return require an indemnity by way of a counter-guarantee bond in its favour from the contractor. The counter-guarantee is equally payable on demand. The defendant concedes in paragraph 21 of its defence that the contractor provided a general counter guarantee and/or indemnity, where the contractor undertook to indemnify the defendant against

all claims and liabilities under any or all the bonds if any. And secondly to deposit with the defendant the full amount of the bond if any within 7 days after request in writing.

The defendant also states in its defence that it would seek to enjoin **Jaswant Singh and brothers Limited** as a 3<sup>rd</sup> party herein seeking indemnity. That was not done and it shows that the defendant has a remedy which is available to it in the event the plaintiff's case succeeds.

As stated earlier, a dispute arose between the plaintiff and the contractor, resulting in the termination of the construction contract. About 6 weeks after the termination of the contract, the plaintiff wrote a letter dated 20<sup>th</sup> February 2006 to the defendant demanding payment of the security under and in accordance with the terms of the performance bond of 24<sup>th</sup> May 2005. It was followed by a formal demand notice by the plaintiff's advocate through a letter dated 12<sup>th</sup> July, 2006.

On 17<sup>th</sup> July 2006 the defendant in admitting its obligations and/or liability and indebtedness to the plaintiff wrote to the contractor demanding immediate payment of the sum of Kshs.6,850,000/= within 7 days, otherwise threatening to take legal action to recover the same at the contractor's expense. A copy of the said letter is also marked to the attention of M/S Muriu Mungai & co. advocates with clear instructions to file suit for the recovery upon expiry of the 7 days notice issued to the contractor. The said letter was also copied to **M/S Covermax Insurance Brokers Limited** asking them to make payments within 7 days, otherwise the defendant would enforce the counter-guarantees.

The letter dated 17<sup>th</sup> July 2006 was written by the legal officer of the defendant company and there is no evidence to show that the said legal officer had no mandate and/or authority to write the said letter. The legal officer draws his mandate from the board of directors and most times from the Executive Officer of the company. It is therefore my firm position that the averment contained in paragraph 8 of the replying affidavit by **Mr. Francis Irungu** is not true. It is not true because the plaintiff has proved beyond any doubt that the bond was signed by an officer of the defendant and before it was issued, the defendant issued an interim cover note pending the issuance of the ultimate performance bond.

The letter dated 17<sup>th</sup> July 2006 by the defendant states in part;

**“performance Bond issued to yourselves in respect of the construction works and services on the Cornerstone apartments situated on L.R. No.209/363/10 Woodlands avenue Nairobi for Gondho Enterprises Ltd,..**

**The said letter was addressed to M/S Jaswant Singh & Brothers Ltd**, the contractor who obtained the performance bond from the defendant in favour of the plaintiff herein. After getting demand notices of the default and/or breach committed by the contractor, the defendant did not cancel or recall the performance bond for cancellation. The respondent has also never written any letter to the applicant to deny liability despite of its receipt of demand letters way back in February and July 2006.

In my understanding performance bond is essentially and ideally meant to cover losses incurred as a result of non performance of a contract by one party. The bond subject to this litigation was made in respect for execution of works referred to as the proposed **Cornerstone** apartments on plot No.209/363/10. Such a document creates an irrevocable obligation in which the defendant is bound to perform unless there is evidence and/or material to show that the bond was fraudulently and illegally obtained from the defendant. The fact that the signatures of **MR. C. N. UMAMAHESWAR** and **E. KABURU** is not denied and/or disputed is a clear testimony that the bond was properly issued by the defendant.

In my humble view, it would be unlawful and wholly inequitable for a party like the defendant who had given an undertaking to remove itself from the obligations and liabilities arising therefrom at the peril of the party who relied on it and without any reasonable justification. Such act would have the effect of undermining and/or destroying the essence of performance bonds in the commercial practice and dealings. The spirit of such contracts is that irrevocable obligations like performance bond are the

lifeblood of international and domestic commerce and except for fraud parties must always respect their contractual rights and liabilities without concern to difficulties in enforcing the same. It is only where there is a clear fraud, where the other party had knowledge which would necessitate the avoidance of such relationship otherwise it is incumbent upon an issuer of a performance bond to always honour it.

It is my judgment that it is fraudulent for the defendant to now turn around and disown the performance bond suddenly later discovering liability had accrued. Let me say that dangerous precedent will be opened by the courts if performance bonds is/are easily swept aside using the defences like the one put forward by the defendant with the sole purpose of frustrating obligations which have accrued.

In High court case **no.94/2007 Milimani Mea Ltd vs Echuka Farm Ltd. & 2 others**, I held;

**“A letter of credit and performance bond is like an undertaking by a bank to meet drafts drawn pursuant to it by the beneficiary of the credit in accordance with the conditions laid down therein. In short the instruments of credit is designed to facilitate trade...It is my position that a letter of credit and/or a performance bond comes into play as a result of a formal written application by the applicant, usually the buyer of goods or seller, which is at the same time a request, a mandate and an indemnity. Thus instructions are the foundation on which the credit itself is based. It is essential that, it would be couched in precise and unambiguous language. It is of course, the actual wording of the credit, no matter what its label, which determines its effect, since a performance bond or a letter of credit is usually restricted on its operation to a particular purpose”.**

The position I expressed in that case was that the court's approach to the enforcement of obligations accruing from instruments of credit and performance bond must be geared towards the enhancement and flow of commercial dealings. The only way out is where there is evidence of fraud committed by one party with the knowledge of another involved in the transaction. It is inappropriate for this court to allow the defendant who gained some benefits by way of premiums to discard his obligations simply because liability has accrued to his side. It is not the case of the defendant that the demand for payment made by the plaintiff is fraudulent. And in my view the only realistic reference to draw is that no fraud legitimate enough to defeat the claim of the plaintiff exists. In my view the issuance of the performance bond which was a prerequisite for the contractor obtaining the construction works from the plaintiff did constitute a bargain between the parties and more so imposed an absolute obligation on the defendant to pay in case he is called upon due to breach/default committed by the contractor. The giving of the performance bond created an elaborate commercial system between the plaintiff, defendant and contractor. And such commercial system created is built upon the footing that the defendant would be called upon to shoulder certain liabilities in case the plaintiff makes out a justifiable cause resulting from a breach committed by the contractor. That has happened and the question of payment of monies under the performance bond is not one between the contractor and the defendant herein.

It is none of the defendant's business to allege that the plaintiff was in breach of the construction contract between it and a 3<sup>rd</sup> party whose remedies were clearly spelt out in the construction contract. The fact that the defendant wishes to seek an indemnity from the contractor is no bar to and does not affect the plaintiff's right to enforce the terms of the performance bond. The defendant issued an interim cover note and had taken steps to claim/sue the contractor to recover the sum secured courtesy of a counter-guarantee whose basis was the performance bond now belatedly impeached.

In a nutshell and having read the defence, replying affidavit, the letter dated 17<sup>th</sup> July 2006 and the performance bond dated 24<sup>th</sup> May, 2005, I am satisfied that the contents considered wholistically amounts to an admission of the claim by the plaintiff. The first prayer for judgment on admission therefore succeeds.

However if I am wrong in that determination, the second point is whether to enter summary judgment as prayed in the plea. In the submission filed herein the defendant contends the performance bond is not sealed by its known common seal and it does not bear the stamp of the defendant, therefore cannot bind the defendant.

In my view person dealing or doing business with a company can only be assumed to be aware of certain public documents of the company. But such parties do not have a legitimate obligation to inquire into the internal dealings or indoor management of the company's transaction. In the replying affidavit of **Mr. Irungu** he says the defendant's directors are not mandated or authorized to issue any performance bond or guarantee on behalf of the defendant. And all documents of such a nature must be executed by two signatories and sealed or stamped with the defendant's common seal or stamp. He also depones that on numerous occasions the defendant's board of directors passed resolutions to the effect that any performance bond or guarantee issued by the defendant be executed by at least two directors or one director together with himself.

I have tried my utmost best to see any averment in the replying affidavit denying the existence and authority of the two person who executed the subject performance bond and regrettably no such allegation exists in the defendant's reply to the application under my determination. In my understanding it is no business of the plaintiff to know whether all or any of the internal regulations had been duly observed by the defendant in giving out the performance bond. The internal dealings and requirement of the defendant company cannot be used to the detriment of outsiders who dealt with the company in, good faith. In my view that is the essence and/or import of what is known as the Turguand's rule in commercial practice. The basis of the Targuand's rule is that a party who relied on a document issued by another party cannot be made to forgo his rights simply because the issuing party thinks certain internal management procedures were not followed. In such instance the company would be assumed to have exercised the act in conformity with its constitution and that the powers have been properly and duly exercised. The rule is designed to protect those who are entitled to assume just because they cannot know the internal procedures of a particular company and whether the person who signed, had the authority which he claims to exercise.

It means it is no business of the plaintiff to know whether the Executive Director who signed the subject performance bond had authority to do so. In any case the defendant in its letter dated 17<sup>th</sup> July 2006 in reply to the two demand notices did not attack the propriety of the performance bond. It had the opportunity to do so, but opted and/or elected not to attack the validity and contents of the bond. The defence raises new issues which were not captured in the letter dated 17<sup>th</sup> July 2006. The defence also introduces the construction contract which has no direct relationship with the bond in issue. The validity of the said contract is not an issue that has fallen for my determination. It is not within the right of the defendant to question a document between the plaintiff and a 3<sup>rd</sup> party. The rights and liabilities as concerns those parties in the contract dated 16<sup>th</sup> May 2005 is distinct and separate from the issues at stake in this matter.

In my view the wheels of business will not go smoothly if the defence put forward by the defendant is entertained. This court cannot allow and/or permit a dereliction of a commercial obligation duly entered or given without any evidence of fraud or misrepresentation. It is also my position that the inadequacy of a document which the party complaining has prepared, cannot be used to defeat the claim of the party who relied on its existence and because of its representation gave a 3<sup>rd</sup> party some benefits which was mandatory in such transaction. That is precisely what happened in this case. I therefore make a finding that there is no triable issue that has been put before me to postpone the day of reckoning.

I agree with the defendant's advocate that the law in summary judgment has been settled for many years but I must add that it is the duty of the defendant to show the existence of a bona fide triable issue which must be allowed to go for hearing. The defendant having given contradictory and disjointed defence cannot be allowed to escape the summary powers of the court. The position of the defendant has been captured by the plaintiff's advocate when he submitted that there is no magic in having a full trial in this dispute. No amount of evidence whether oral or otherwise would change the defendant's express admission as contained in the letter dated 17<sup>th</sup> July 2006. The said admission and/or acknowledgement is not denied in the defence. It is also not denied in the sketchy replying affidavit by **Mr. Irungu**.

In the premises the application also succeeds in that second limb. There is no need for me to consider the 3<sup>rd</sup> prayer in the application. **All in all my decision is to allow the application in terms of prayer No.1**

**plus costs and interest at court rate. The plaintiff shall also have the costs of the suit since this application has conclusively determined the whole dispute in a final manner.**

Dated , signed and delivered at Nairobi this 20<sup>th</sup> day of February, 2008.

**M. A. WARSAME**

**JUDGE**

**Court:** Ruling delivered in the presence of **Mr. Maweu** for the plaintiff and **Mr. Welimo** for the defendant in open court.

**M. A. WARSAME**

**JUDGE**