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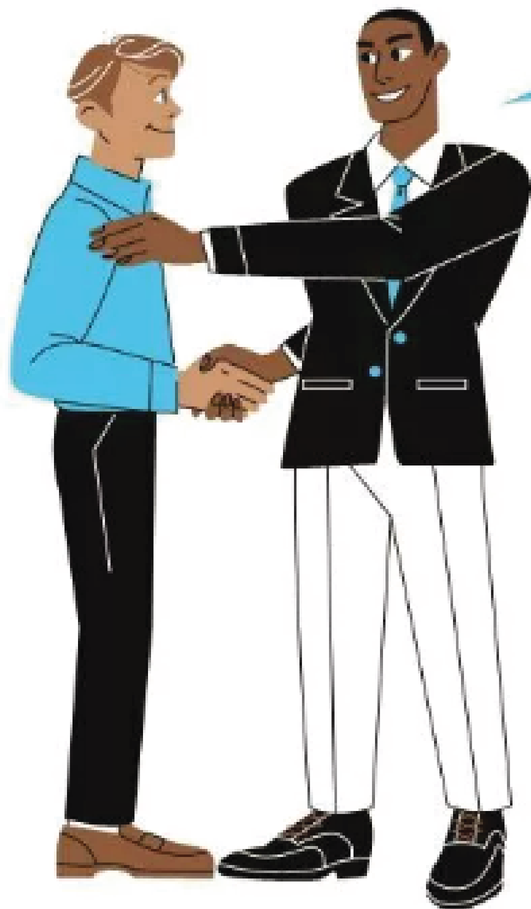
Contracts of Guarantee
The law and practice in Uganda



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1 Introduction

When someone acts as a guarantor for a loan or any other financial obligation, they assume the responsibility of paying back the debt if the borrower fails to do so. This is a significant obligation, as the guarantor may be required to pay back the full amount of the loan, plus any interest and fees that have accrued. As we discuss in this article, potential guarantors must understand their responsibilities and liabilities before entering into such arrangements, especially since courts tend to interpret strictly the terms of guarantee arrangements.

2. Definition

A contract of guarantee, as defined in Uganda's Contract Act of 2010, refers to an agreement, whether oral or written, to discharge the liability of a third party in case of default. As was held in the case of Alice Norah Mukasa v Centenary Bank Limited & Anor High Court Civil Suit No.77 of 2010, a guarantor assures the lender that they will pay in case the borrower fails to repay the loan. Similarly, in Paul Kasagga and Anor v Barclays Bank (U) Ltd (HCT-00-CC-MA 113 of 2008), the court noted that the guarantor undertakes to ensure that the principal debtor fulfills their obligation to the creditor and becomes liable if they fail to do so.

3. Form of agreement

There is a contradiction in the law regarding the form contracts of guarantee must take. While section 10(6) of the Contract Act stipulates that a contract of guarantee must be in writing, section 68 provides that such contracts can either be oral or written. This has, however, been harmonized by Justice Madrama in the case of Karangwa Joseph v Kulanju Willy (High Court Civil Appeal) No.3 of 2016, explaining that an oral contract of guarantee can be used for values of up to 25 currency points, while contracts of higher value must be in writing. Although oral contracts are permissible in some circumstances, it is advisable to reduce the agreement to writing to avoid uncertainty and disputes over the terms of the contract.

4. Tripartite arrangement

Contracts of guarantee involve three parties, namely the creditor, principal debtor, and guarantor, each with a specific obligation. The creditor provides the credit, the principal debtor repays the creditor, and the guarantor assumes the principal debtor's obligations in the event of loan default. It is also important to note that the principal debtor must indemnify the guarantor for any losses resulting from the debtor's default.

5. Guarantor liability

As enumerated in the cases of Paul Kasagga and Anor v Barclays Bank (U) Ltd (HCT-00-CC-MA 113 of 2008) and Bank of Uganda v Banco Arabe Espanol, Civil Appeal No. 23 of 2000, guarantor responsibility is based on the principal debtor's liability and comes into effect when the principal debtor defaults, usually after receiving a notice of default.

a) *Joint and several*

The guarantor's role is to assure the lender of loan repayment in case of borrower default. Both parties, i.e., the principal debtor and the guarantor, are jointly and severally liable to pay the loan. This means they can be pursued separately or together for any outstanding balance.

b) *Several guarantors*

Where there is more than one guarantor, courts have noted that, for as long as there is money due and owing to the creditor, all guarantors are jointly and severally liable to the creditor insofar as the recovery of outstanding sums is concerned. The creditor can pursue all the guarantors and the principal debtor jointly or separately in different kinds of proceedings. See Mian Aqueel & Anor v Exim Bank (U) (Ltd) (Miscellaneous Application 497 of 2017)."

c) *Liability amidst distress*

Courts have held that a winding-up or receivership action against the principal debtor does not prevent any claim against the guarantors as long as there is an outstanding debt owed to the creditor. The extent of the guarantors' liability in such cases is determined by the specific terms of the guarantee agreement. See Barclays Bank of Uganda Ltd v Jing Hong and Guo Dong; Civil Suit 35 of 2009 and Mian Aqueel & Anor v Exim Bank (U) (Ltd) (Miscellaneous Application 497 of 2017)."

6. Discharge from liability

Discharge of guarantor liability refers to the release of the guarantor from their financial responsibility for the underlying debt. This can be achieved in several ways as discussed below.

a) *Release of the principal debtor*

As a general rule, a guarantor is discharged from liability against the creditor once the principal debtor clears own debt obligations.

b) *Creditor omission or commission*

Where a creditor commits or omits to do an act that is ultimately injurious to the rights of the guarantor, then the guarantor will be discharged. For instance, if the creditor has a duty such as registering a security and fails and eventually impedes the rights of a creditor to act on that security.

Citing the decision in China and South Sea Bank Ltd Vs Tan [1989] 3 All ER 839, the High Court of Uganda in the matter of Stanbic Bank Limited v Cellular Galore & 2 others High Court Civil Suit No. 50 of 2010 noted that " the rule upon the subject seems to be that if the person guaranteed does any act injurious to the surety, or inconsistent with his rights or if he omits to do any act which his duty enjoins him to do, and the omission proves injurious to the surety then the surety will be discharged... the rights of a surety depend rather on principles of equity than upon the actual contract".

c) *Contract variation*

Where there is any variation to the terms of the contract between a creditor and principal debtor without the consent of the guarantor, the guarantor is discharged from subsequent material transactions.
In Holme v Brunskill CA 1877 cited with approval in Anupama Rao Singh V Giuseppe Giamona & Claudio Nocotra; High Court Civil Suit No.120 of 2013, it was stated that, a guarantor is released from liability under a guarantee given to a creditor where that creditor and the principal debtor have entered into an agreement, subsequent to the giving of the guarantee, which has the effect of altering the contractual position between them, to the disadvantage of the guarantor, without his prior consent.

It could also be a situation where the creditor enters into a compromise with the principal debtor granting more time to pay or commitment not to sue him/her for the loan recovery, the guarantor stands discharged from his/her obligations unless the guarantor assents to the arrangement.

7. Guarantor rights upon settlement

Where the principal debtor defaults and the guarantor makes payment to the creditor on their behalf, the law affords protection to the guarantor by giving them avenues through which they can reclaim the money paid to settle the principal debtor's obligation.
The guarantor will, in this case, have the rights that accrued to the creditor which include indemnity, set off, and subrogation amongst other rights against the principal debtor. These are aimed at ensuring that the guarantor is not left without any remedy against an unscrupulous principal debtor.

8. Conclusion

Contracts of guarantorship are vital legal instruments that minimize the risk of default to creditors while enabling businesses to access necessary capital and credit for operations. To abate disputes, parties must approach them with diligence, seek third-party perspectives, and fully comprehend their obligations and potential consequences.

Cristal Advocates accepts no responsibility for any loss occasioned to any person acting or refraining from acting as a result of material contained in this publication. Further advice should be taken before relying on the contents of this publication.

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At Deloitte, he lived and worked in Uganda, Kenya, Tanzania and the United Kingdom for over 6 years and subsequently became the firm's chief of staff for the Energy and Resources Industry Group seeing him play a lead advisory role in Uganda, Kenya, Tanzania, Mozambique, South Sudan, Somalia and Ethiopia.

Denis is widely published and a regular commentator in the local, regional and international media and speaker at various forums regarding the taxation and financing of energy projects as well as the protection of large capital projects within the framework of international investment law.

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Bill is a Senior Advisor with Cristal Advocates. He has concentrated on working with energy companies with a particular focus on cross border transactions and M&A since 1989 and is a leading global energy and tax practitioner with wide international experience. Between 1986 and 1998, he worked in London with the UK tax authorities and Big Four accounting firms. From 1998 to 2004, he was based in Kazakhstan working across the Caspian region with Deloitte. He was in the region at the time it was developing its infrastructure for crude oil production with international investment following the collapse of the Soviet Union.

From 2004 to 2008, he worked in Russia where he led Deloitte's oil and gas industry group and established Deloitte's office in Sakhalin. He moved to East Africa in 2009 leading Deloitte's energy and resources industry group in Uganda, Kenya, Tanzania, Rwanda, Ethiopia and Mozambique. He was initially based in Kampala, Uganda later relocating to Dar es Salaam, Tanzania. Bill returned to the UK in 2014 supporting Deloitte UK teams working on outbound projects investing in Africa and was a key member of Deloitte UK's energy and resource practice until his retirement from the firm in September, 2018.

Bill is a graduate of Oxford University and completed his inspectors' training with the UK Inland Revenue in 1989. ■

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John leads the public policy and advocacy practice at the firm and combines unique public and private sector experience.

Prior to joining Cristal Advocates, he had worked as a Private Secretary to the President of the Republic of Uganda. During this time, he participated in several public and private sector engagements that included advising and coordinating activities relating to oil and gas as well as infrastructural projects of national significance. John had earlier worked with the Post Bank Uganda Limited and Shonubi Musoke and Co. Advocates.

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Dickens leads the oil and gas practice at Cristal Advocates. He has an in depth appreciation of Uganda's oil and gas sector having served as the maiden Company Secretary of the Uganda National Oil Company (UNOC) and the Uganda Refinery Holding Company Limited (URHC). UNOC represents the Government of Uganda commercial interests in the oil and gas sector while URHC represents government interests in the refinery project as well as managing the petrol based industrial park.

Dickens was instrumental in UNOC's formation and initial period of operation and also served as its head of Contracts, Negotiations and Advisory until May 2018. Prior to joining UNOC, Dickens was Legal Counsel at the Petroleum Directorate of the Ministry of Energy playing key legal advisory roles on the negotiation and implementation of PSAs, Joint venture and other oil and gas agreements. He was also part of the team that shepherded the process of enacting the current Ugandan oil and gas Legislations and Regulations including the local content requirements.

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He joined Cristal Advocates from Kizza, Tumwesige, and Ssemambo Advocates. He previously worked with the Advocates Coalition for Development and Environment (ACODE). He also undertook a traineeship with the oil and gas division of Webber Wetzel in Johannesburg, South Africa.

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